MORTGAGE ORIGINATION: THE IMPACT OF RECENT CHANGES ON HOMEOWNERS AND BUSINESSES

HEARING

BEFORE THE

SUBCOMMITTEE ON
INSURANCE, HOUSING AND
COMMUNITY OPPORTUNITY

OF THE

COMMITTEE ON FINANCIAL SERVICES
U.S. HOUSE OF REPRESENTATIVES

ONE HUNDRED TWELFTH CONGRESS

FIRST SESSION

JULY 13, 2011

Printed for the use of the Committee on Financial Services

Serial No. 112–47

U.S. GOVERNMENT PRINTING OFFICE

67–942 PDF WASHINGTON : 2012

For sale by the Superintendent of Documents, U.S. Government Printing Office
Internet: bookstore.gpo.gov Phone: toll free (866) 512–1800; DC area (202) 512–1800
Fax: (202) 512–2104 Mail: Stop IDCC, Washington, DC 20402–0001

HOUSE COMMITTEE ON FINANCIAL SERVICES

SPENCER BACHUS, Alabama, *Chairman*

JEB HENSARLING, Texas, *Vice Chairman*
PETER T. KING, New York
EDWARD R. ROYCE, California
FRANK D. LUCAS, Oklahoma
RON PAUL, Texas
DONALD A. MANZULLO, Illinois
WALTER B. JONES, North Carolina
JUDY BIGGERT, Illinois
GARY G. MILLER, California
SHELLEY MOORE CAPITO, West Virginia
SCOTT GARRETT, New Jersey
RANDY NEUGEBAUER, Texas
PATRICK T. McHENRY, North Carolina
JOHN CAMPBELL, California
MICHELE BACHMANN, Minnesota
THADDEUS G. McCOTTER, Michigan
KEVIN McCARTHY, California
STEVAN PEARCE, New Mexico
BILL POSEY, Florida
MICHAEL G. FITZPATRICK, Pennsylvania
LYNN A. WESTMORELAND, Georgia
BLAINE LUETKEMEYER, Missouri
BILL HUIZENGA, Michigan
SEAN P. DUFFY, Wisconsin
NAN A. S. HAYWORTH, New York
JAMES B. RENACCI, Ohio
ROBERT HURT, Virginia
ROBERT J. DOLD, Illinois
DAVID SCHWEIKERT, Arizona
MICHAEL G. GRIMM, New York
FRANCISCO "QUICO" CANSECO, Texas
STEVE STIVERS, Ohio
STEPHEN LEE FINCHER, Tennessee

BARNEY FRANK, Massachusetts, *Ranking Member*
MAXINE WATERS, California
CAROLYN B. MALONEY, New York
LUIS V. GUTIERREZ, Illinois
NYDIA M. VELÁZQUEZ, New York
MELVIN L. WATT, North Carolina
GARY L. ACKERMAN, New York
BRAD SHERMAN, California
GREGORY W. MEEKS, New York
MICHAEL E. CAPUANO, Massachusetts
RUBÉN HINOJOSA, Texas
WM. LACY CLAY, Missouri
CAROLYN McCARTHY, New York
JOE BACA, California
STEPHEN F. LYNCH, Massachusetts
BRAD MILLER, North Carolina
DAVID SCOTT, Georgia
AL GREEN, Texas
EMANUEL CLEAVER, Missouri
GWEN MOORE, Wisconsin
KEITH ELLISON, Minnesota
ED PERLMUTTER, Colorado
JOE DONNELLY, Indiana
ANDRÉ CARSON, Indiana
JAMES A. HIMES, Connecticut
GARY C. PETERS, Michigan
JOHN C. CARNEY, JR., Delaware

LARRY C. LAVENDER, *Chief of Staff*

SUBCOMMITTEE ON INSURANCE, HOUSING AND COMMUNITY OPPORTUNITY

JUDY BIGGERT, Illinois, *Chairman*

ROBERT HURT, Virginia, *Vice Chairman*
GARY G. MILLER, California
SHELLEY MOORE CAPITO, West Virginia
SCOTT GARRETT, New Jersey
PATRICK T. McHENRY, North Carolina
LYNN A. WESTMORELAND, Georgia
SEAN P. DUFFY, Wisconsin
ROBERT J. DOLD, Illinois
STEVE STIVERS, Ohio

LUIS V. GUTIERREZ, Illinois, *Ranking Member*
MAXINE WATERS, California
NYDIA M. VELÁZQUEZ, New York
EMANUEL CLEAVER, Missouri
WM. LACY CLAY, Missouri
MELVIN L. WATT, North Carolina
BRAD SHERMAN, California
MICHAEL E. CAPUANO, Massachusetts

CONTENTS

WITNESSES

WEDNESDAY, JULY 13, 2011

APPENDIX

ADDITIONAL MATERIAL SUBMITTED FOR THE RECORD

MORTGAGE ORIGINATION: THE IMPACT OF RECENT CHANGES ON HOMEOWNERS AND BUSINESSES

Wednesday, July 13, 2011

U.S. HOUSE OF REPRESENTATIVES,
SUBCOMMITTEE ON INSURANCE, HOUSING
AND COMMUNITY OPPORTUNITY,
COMMITTEE ON FINANCIAL SERVICES,
Washington, D.C.

The subcommittee met, pursuant to notice, at 2:15 p.m., in room 2128, Rayburn House Office Building, Hon. Judy Biggert [chairwoman of the subcommittee] presiding.

Members present: Representatives Biggert, Hurt, Miller of California, Duffy, Dold, Stivers; Gutierrez, Waters, Clay, Watt, and Sherman.

Also present: Representative Green.

Chairwoman BIGGERT. This hearing of the Subcommittee on Insurance, Housing and Community Opportunity will come to order. I thank all the witnesses for waiting. We always have these pesky votes in the afternoon. I am sorry to keep you waiting. We are going to start, even though we don't have very many members here. We do have two panels and lots of witnesses, so we want to give you the time to speak and then to have questions.

Without objection, all members' opening statements will be made a part of the record, and I will recognize myself for 5 minutes.

Good afternoon, and thank you for attending today's hearing entitled, "Mortgage Origination: The Impact of Recent Changes on Homeowners and Businesses." I would like to welcome today's witnesses, and given that we have such a large number of witnesses, I will be brief. I would ask that others do the same so that members have time to ask our witnesses questions.

Today's hearing is about jobs, the recovery and future of the housing and mortgage markets, as well as consumer access to credit services and useful information.

As we did during our first hearing of the 112th Congress, this subcommittee will continue to focus on regulatory barriers to the housing market recovery, barriers that include policies that limit the availability of credit, raise costs for consumers, and add uncertainty to this already fragile recovery.

With that, I recognize the gentleman from Illinois for 5 minutes.

Mr. DOLD. Thank you, Chairwoman Biggert. I certainly appreciate the time, and I want to thank the panelists for taking your time to come and join us today.

Congress has an obligation to continually review and reevaluate existing laws and regulations to determine if they are working, have they done what they were intended to do, what unintended negative consequences or unanticipated consequences have resulted, and have the legislative and regulatory costs exceeded the corresponding benefits.

Historically, Congress has performed this continual review and reevaluation obligation far too infrequently, but I am pleased to see that the committee and this subcommittee in particular take the congressional obligation seriously under the leadership of Chairman Bachus and Chairwoman Biggert. That is why Chairwoman Biggert has called this hearing, to perform our congressional obligation to review and to reevaluate the Dodd-Frank rules and the corresponding regulations relating to mortgage origination.

More specifically, we are here to evaluate the rules and the regulations relating to mortgage disclosure, home warranties, repayment ability standards, risk retention rules, loan originator compensation, and appraisal reforms. Are the Dodd-Frank provisions and the corresponding regulations working, are they likely to work or are they having or likely to have unintended negative consequences, and are their costs likely to exceed their benefits? Are they promoting or hindering private sector job growth, capital investment, credit availability, and overall economic growth?

The answers to these important questions can dramatically affect small business, of which I am a small business employer. They can also affect employment, consumers and borrowers, the mortgage finance and real estate markets, and our economy as a whole.

So, I thank Chairwoman Biggert for holding this important hearing, and I thank the witnesses for your time and for your testimony. I yield back the balance of my time.

Chairwoman BIGGERT. Thank you, Mr. Dold. Mr. Hurt, do you have a statement?

Mr. HURT. I do not.

Chairwoman BIGGERT. Then, we will start with our first panel. We have a great panel: Ms. Sandra Braunstein, Director of the Division of Consumer and Community Affairs, Board of Governors of the Federal Reserve System; the Honorable Teresa Payne, Deputy Assistant Secretary, Office of Regulatory Affairs, U.S. Department of Housing and Urban Development; Ms. Kelly Cochran, Deputy Assistant Director, the Office of Regulations, Consumer Financial Protection Bureau (CFPB), U.S. Department of the Treasury; Mr. James Park, Executive Director, Appraisal Subcommittee, Federal Financial Institutions Examination Council; Mr. William Shear, Director, Financial Markets and Community Investment, U.S. Government Accountability Office; and Ms. Anne Norton, Maryland Deputy Commissioner of Financial Regulation, on behalf of the Conference of State Bank Supervisors.

Welcome to you all. As you know, without objection, your written statements will be made a part of the record, and you will each be recognized for a 5-minute summary of your testimony. Then, we will recognize the members for 5 minutes each to ask questions in the same order as opening statements.

Mr. Gutierrez, would you like to give an opening statement?

I recognize Mr. Gutierrez for 5 minutes.

Mr. GUTIERREZ. Good afternoon, and thank you, Chairwoman Biggert, for holding this hearing on mortgage origination. I would like to welcome the witnesses here today.

It has been almost a year since this Chamber passed the historic Wall Street Reform and Consumer Protection Act, or Dodd-Frank. These past few months have been especially critical to the implementation of many important provisions.

For the first time in the history of the United States, and thanks to the passage of Dodd-Frank, an agency has been created to specifically serve and assist and, most importantly, protect American consumers from the unfair and abusive practices of financial services providers. The Consumer Financial Protection Bureau is a central provision in Dodd-Frank and is expected to provide a crucial role to protect consumers and help ensure that our country never finds itself on the brink of economic collapse.

Undoubtedly, the rulemaking period for provisions in Dodd-Frank that deals with ameliorating our housing system and the transfer of authority of many of these provisions to the CFPB, which we will discuss today, is exceptionally important to the national recovery.

In approximately a week, many important activities will be transferred to the CFPB. This agency will be responsible for overseeing the regulations that will address and reform the abusive and deceptive practices in our Nation's housing industry. I would like to commend the CFPB for measures they have already taken to develop a single, more streamlined, user-friendly mortgage disclosure form and for engaging key industry representatives and consumer advocates in that process.

I would like to enter into the record an article from the American Banker that further highlights the CFPB's leadership and diligence on this issue.

Chairwoman BIGGERT. Without objection, it is so ordered.

Mr. GUTIERREZ. The CFPB will become a vital agency in handling many important and necessary proposals that were included in Dodd-Frank and which, once fully implemented, will address the Nation's housing crisis and will help American homeowners during the most devastating economic downturn.

I look forward to hearing the thoughts and opinions of our witnesses here today and I thank the chairwoman.

Chairwoman BIGGERT. Thank you, Mr. Gutierrez.

Ms. Braunstein, you are recognized for 5 minutes.

STATEMENT OF SANDRA F. BRAUNSTEIN, DIRECTOR, DIVISION OF CONSUMER AND COMMUNITY AFFAIRS, BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM

Ms. BRAUNSTEIN. Thank you.

Chairwoman Biggert, Ranking Member Gutierrez, and members of the subcommittee, I appreciate the opportunity to appear today to discuss regulatory actions taken by the Federal Reserve in the home mortgage markets. Our goal has been to craft clear rules that deter abuses and enhance consumer protections while preserving responsible lenders' ability to meet the needs of all segments of the market.

During the past 3 years, the Board addressed the need for mortgage reform by issuing seven final rules under the Truth in Lending Act and the Home Ownership and Equity Protection Act, plus five additional proposed rules that will become the responsibility of the Consumer Financial Protection Bureau. These 12 rulemakings cover all stages of the mortgage lending process.

In July 2008, the Board issued rules establishing new consumer protections for residential mortgages. For higher-priced loans, the rules strengthened underwriting requirements, restricted prepayment penalties, and required escrow accounts. Other protections were applied to the entire mortgage market to address issues with appraisals, advertising, loan servicing, and the need for earlier cost disclosures.

In September 2010, the Board issued final rules prohibiting unfair practices relating to loan originator compensation. The Board had initially proposed a disclosure-based solution, but withdrew that proposal in 2008 after consumer testing showed that disclosures were ineffective. The final rules regulate the manner in which loan originators may be compensated, but not the amount.

The rule also prohibits originators from steering consumers to loans which increase the originator's compensation but are not in the consumer's interest. The DFA also addresses these concerns, and after enactment the Board decided to finalize its proposed rules as the best way to effectuate that law's legislative purpose and eliminate these unfair practices without further delay. The Board recognizes, however, that there are some additional requirements in the DFA which will require subsequent rulemaking by the Bureau.

In 2008, the Board issued rules to strengthen the property valuation process by prohibiting coercion of appraisers. The DFA codified the anti-coercion provisions in the Board's rules while also including a provision requiring that independent appraisers receive customary and reasonable compensation. The statute directed the Board to issue interim final rules implementing these requirements within 90 days, which the Board did in October 2010.

Going forward, the Board, the other Federal banking agencies, the Federal Housing Finance Agency, and the Bureau will share responsibility for jointly issuing permanent rules on appraisal independence.

In March 2011, the Board issued a final rule to implement a provision of the DFA that increased the annual percentage rate threshold used to determine whether a mortgage lender is required to establish an escrow account for jumbo mortgage loans. Also in March, the Board proposed Dodd-Frank mandated rules for escrow accounts that add new disclosures and expand the mandatory escrow period from 1 to 5 years. The proposal would also exempt creditors from the escrow requirements if they operate predominantly in rural or underserved areas and originate a limited number of loans that are held in portfolio.

In April 2011, the Board published proposed rules under the DFA to strengthen mortgage underwriting. The proposal provides options for creditors to meet the requirement that they make a reasonable and good faith determination that the consumer will have the ability to make the scheduled payments. The Bureau will assume responsibility for developing final rules.

During 2009 and 2010, the Board issued three regulatory proposals to improve disclosures for closed-end mortgages, HELOCs, and reverse mortgages. In February, the Board announced that these pending disclosure rulemakings would be transferred to the Bureau.

Consumer protection remains important to the Board, notwithstanding the upcoming transfer of various rule-writing authorities to the Bureau. During the mortgage crisis, we have witnessed the importance of effective consumer protection, not only in preserving the well-being of particular communities, but more importantly to the economy as a whole. The effectiveness of the regulations depends critically on strong supervision and enforcement. The Federal Reserve retains a significant responsibility in supervising financial institutions, which we will continue to take seriously.

Thank you very much. I look forward to your questions.

[The prepared statement of Ms. Braunstein can be found on page 80 of the appendix.]

Chairwoman BIGGERT. Thank you.

Ms. Payne, you are recognized for 5 minutes.

STATEMENT OF TERESA B. PAYNE, ASSOCIATE DEPUTY ASSISTANT SECRETARY, REGULATORY AFFAIRS, U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT

Ms. PAYNE. Thank you, Chairwoman Biggert, Ranking Member Gutierrez, and members of the subcommittee for this opportunity to testify today.

My name is Teresa Payne, and I am the Associate Deputy Assistant Secretary for Regulatory Affairs at HUD with responsibility over RESPA, ILS, the SAFE Act, and manufactured housing. I have been working at the Department for nearly 15 years, during which I have spent a significant amount of time on RESPA policy enforcement issues. It is my pleasure to bring you up to date on the status of RESPA and the transition of its statutory authority from HUD to the CFPB.

Let me begin by first bringing you up to date on the current status of RESPA at HUD, HUD's work on regulating home warranties under RESPA, and the transition to the CFPB.

While we have been preparing for our authority and staff to move over to the CFPB, we have been hard at work administering RESPA through policy and enforcement actions. During 2010 and 2011, the RESPA complaint caseload in the office of RESPA has been extremely heavy. More than 1,500 cases were opened in the last 18 months. The office's increased caseload has led to greater coordination with State regulators, the Department of Justice, and HUD's own OIG.

As you are aware, in November 2008, the Department issued a new RESPA regulation that established a standard required GSE form, a revised and expanded HUD-1 settlement statement, and a new settlement cost booklet.

To be in compliance with RESPA and help assure fair prices for consumers, actual costs at closing must fall within established tolerance ranges for the first time. The new disclosures were implemented on January 1, 2010. The RESPA office established a compliance guidance regiment to educate all interested stakeholders. This included speaking to over 175 organizations, periodically publishing on its Web site, the RESPA Roundup, which is a newsletter to address relevant compliance questions, and issuing on its Web site over 300 frequently asked questions and answers.

In order to reach out directly to better inform consumers, the RESPA office also produced and released three consumer education videos: Shopping for Your Home; Shopping for a Loan; and Closing the Deal.

Although it hasn't been long since the completion of the 2010 implementation year, some tangible results are being seen. Prospective borrowers are receiving more accurate GSE, and costs at closing are being held within tolerance ranges.

Several interpretive rules and policy pieces have been published during the last 18 months. I would like to highlight just a few. Home warranties have been expressly covered as a settlement service under HUD's regulations since 1992. In June 2010, HUD issued an interpretive rule regarding compensation arrangements for real estate agents in connection with the sale of home warranties. This rule clarified circumstances under which a real estate agent may be compensated for the sale of home warranties under RESPA. Although not required, HUD also invited public comment on the clarity and scope of the rule. Based on the comments received, the Department published additional clarifying guidance.

Additionally, you have asked HUD to review and comment on the recently proposed legislation entitled the RESPA Home Warranty Clarification Act of 2011. While the Administration has not taken a formal position on the bill, HUD has preliminary concerns that the proposed legislation could limit consumer protection in the context of home warranties and lead to higher closing costs for consumers through referral fees. HUD recommends that prior to enacting legislation, a study be conducted by appropriate regulatory agencies about the sale of home warranties, representations made by real estate professionals to consumers about what the home warranty covers, and the underlying terms of the contract.

While we are preparing for our impending transfer to the CFPB, we continue to work diligently on enforcement. This week, we announced a settlement with Fidelity National Financial for $4.5 million for RESPA violations. Just this morning, we announced a settlement with Prospect Mortgage in the amount of $3.1 million for creating sham affiliated businesses through limited liability companies.

I would like to turn now to the question of the transfer of RESPA-related functions and personnel to the CFPB. Please note that I am still an employee of HUD and will not be an employee of the CFPB until July 31st. Therefore, I am not authorized to speak on behalf of the CFPB.

As you know, next week the statutory authority for RESPA will formally transfer from HUD to the CFPB, and 37 HUD employees are currently slated to become CFPB employees by July 31st. HUD has been working diligently with the CFPB to make the transition of documents, IT systems, and personnel as smooth and seamless as possible.

Thank you again for this opportunity to appear before you today, and I look forward to answering any questions you may have.

[The prepared statement of Ms. Payne can be found on page 192 of the appendix.]

Chairwoman BIGGERT. Thank you, Ms. Payne.

Ms. Cochran, you are recognized for 5 minutes.

STATEMENT OF KELLY THOMPSON COCHRAN, DEPUTY ASSISTANT DIRECTOR, OFFICE OF REGULATIONS, CONSUMER FINANCIAL PROTECTION BUREAU, U.S. DEPARTMENT OF THE TREASURY

Ms. COCHRAN. Thank you. Thank you, Chairwoman Biggert, Ranking Member Gutierrez, and members of the subcommittee for inviting me to testify today about the work of the Consumer Financial Protection Bureau. On behalf of the CFPB, I appreciate this opportunity to update you about our work on simplifying mortgage disclosures.

Last year, the Dodd-Frank Act both created the Bureau and directed the Bureau to develop integrated disclosure forms that would satisfy the requirements of both the Truth in Lending Act and the Real Estate Settlement Procedures Act. Merging these two disclosure regimes has been the focus of legislative and regulatory activity since 1996, and the Dodd-Frank Act directs the Bureau to propose integrated reforms and related regulations by July 21, 2012. At the Bureau, we have made this project one of our top priorities and we have conducted extensive outreach to industry, consumer advocacy groups, and other stakeholders to get a clear picture of issues regarding the current forms.

I was pleased to participate in May in a bipartisan CFPB briefing with staff of this committee, and we appreciate the opportunity to update you today on our work on this important undertaking.

The Dodd-Frank Act sets two purposes for the integrated disclosures. The first is to aid consumer understanding by using readily understandable language, and the second is to facilitate compliance with TILA and RESPA. Our goal here is shorter, clearer forms, the kind that on the one hand, make it easier for consumers to understand key loan terms and to compare offers to find a loan that best meets their needs, and on the other hand, reduce unwarranted regulatory burdens for lenders and other industry participants.

We started work on the disclosure project with a roundtable at the Treasury Department last fall that brought together industry and consumer advocates to discuss ways to simplify the disclosures. In the months since, we have reviewed research, we have conducted extensive additional outreach, and we have begun the process of design and analysis. Our outreach has included meetings with all sectors of industry, with document service providers and other technology support companies, consumer advocacy groups and housing counselors, Federal and State regulators, and academic researchers.

In May, we released two prototypes for the combined mortgage disclosures that must be provided 3 days after application. We tested the two drafts through one-on-one interviews with consumers, lenders, and brokers. In addition, we posted the prototypes on our Web site to gather broad-based public input through an interactive

Web tool. More than 13,000 users responded to this process with written feedback to the initiative, which we are calling the "Know Before You Owe Project." Based on the results of the initial testing and the public feedback, we revised the draft disclosures and released a second round of prototypes in late June. We have now completed testing on the second round and received related feedback from nearly 4,000 users via our Web site.

To our knowledge, we are the first Federal financial services agency is to seek such broad-based public input this early in the design process before proposing a rule for a consumer disclosure. This is a learning process for us and for the participants, and we are very encouraged by the response to date. We believe this process can be particularly useful in identifying potential implementation issues that may arise for different kinds of financial service providers and in helping us to address those issues as we move along in the design process.

Looking ahead, we expect to conduct several additional rounds of revision and testing into the fall. We will accelerate work on the underlying regulations and on developing integrated closing stage disclosures. We also expect to convene a panel to consult with small businesses regarding potential impacts prior to composing a rule and to consult with prudential regulators and other appropriate agencies.

In conclusion, Chairwoman Biggert, Ranking Member Gutierrez, and members of the subcommittee, thank you again for inviting me to testify today about our work on this project. We know that no one initiative can solve all issues regarding mortgage originations, but we remain convinced that simple, streamlined disclosures are a critical piece that can both provide more value to consumers and reduce burden to lenders.

We welcome the opportunity to discuss our efforts and further update you on our progress and we welcome any questions. Thank you.

[The prepared statement of Ms. Cochran can be found on page 114 of the appendix.]

Chairwoman BIGGERT. Thank you.

Mr. Park, you are recognized for 5 minutes.

STATEMENT OF JAMES R. PARK, EXECUTIVE DIRECTOR, APPRAISAL SUBCOMMITTEE, FEDERAL FINANCIAL INSTITUTIONS EXAMINATION COUNCIL

Mr. PARK. Good afternoon. Thank you, Chairwoman Biggert, Ranking Member Gutierrez, and members of the subcommittee. The Appraisal Subcommittee appreciates the opportunity to provide information about its mission and current activities on behalf of the Chairman of the Federal Financial Institutions Examination Council. My testimony today does not necessarily represent the views of the Council or the Appraisal Subcommittee. Today, I will give you a brief history of the Appraisal Subcommittee, commonly known as the ASC, and describe its primary responsibilities.

Congress passed Title XI of the Financial Institutions Reform Recovery and Enforcement Act to address identified weaknesses regarding real property appraisals. This law created the ASC as an entity within the Council. In general, the ASC operates independently of the Council.

The law created a regulatory framework that involves the following private, State, and Federal entities: The Appraisal Foundation, a private nonprofit, is the parent organization for the Appraisal Standards Board and Appraiser Qualifications Board. These Boards respectively issue the uniform standards of professional appraisal practice and the real property appraiser qualification criteria.

The State programs regulate appraisers in the 50 States, the District of Columbia, and 5 territories. The Federal financial institutions regulatory agencies are responsible for prescribing appropriate standards for the performance of appraisals, and the ASC provides Federal monitoring support and oversight to both the private and State entities.

The ASC Board is made up of seven members designated by each of the Federal financial institutions' regulatory agencies, the Department of Housing and Urban Development, and pursuant to Dodd-Frank, the Federal Housing Finance Agency, and the Consumer Financial Protection Bureau.

The primary responsibilities of the ASC include monitoring the State programs and maintaining a national registry of appraisers. Users of the national registry can easily determine whether an appraiser is eligible to perform appraisals for federally-related transactions and view their disciplinary histories. The ASC also monitors and reviews the Appraisal Foundation and provides grants to the foundation to defray costs relating to the activities of the Appraisal Standards Board and the Appraisal Qualifications Board.

Dodd-Frank expanded the ASC's mission and authority. Actions already taken pursuant to Dodd-Frank include: increasing the national registry fee from $25 to $40 effective January 1, 2012; adding the Federal Housing Finance Agency to the ASC; and determining that a national appraisal complaint hotline does not exist. The ASC is currently studying various options for the establishment of such a hotline.

Dodd-Frank also required the adoption of several other reforms, for example, regulation of appraisal management companies. In general, appraisal management companies provide regional and national third party valuation services. The ASC will monitor State registration and supervision of appraisal management companies and maintain a national registry once regulations setting minimum requirements are promulgated as required by Dodd-Frank. The ASC 2010 annual report gives a more detailed overview of this and other Dodd-Frank amendments to Title XI.

State programs are assessed every 2 years through an onsite compliance review process. Last year marked the second full year the ASC conducted State compliance reviews under a revised process and with positive results. The ASC may take action against a State in the case of noncompliance which historically was limited to an order of non-recognition. Such an order would severely affect mortgage lending in the State.

The regulatory reforms developed by Chairwoman Biggert and former Congressman Kanjorski that eventually became part of Dodd-Frank provide the ASC with additional tools that can assist the agency's oversight of the appraisal process, thereby leading to improvement in appraisal credibility and consumer confidence in appraisals. The ASC is dedicated to carrying out its new and existing Title XI mandates transparently and efficiently.

In conclusion, I again appreciate the opportunity to appear before the subcommittee and look forward to addressing your questions.

[The prepared statement of Mr. Park can be found on page 179 of the appendix.]

Chairwoman BIGGERT. Thank you, Mr. Park.

Mr. Shear, you are recognized for 5 minutes.

STATEMENT OF WILLIAM B. SHEAR, DIRECTOR, FINANCIAL MARKETS AND COMMUNITY INVESTMENT, U.S. GOVERNMENT ACCOUNTABILITY OFFICE

Mr. SHEAR. Chairwoman Biggert, Ranking Member Gutierrez, and members of the subcommittee, I am pleased to be here today to discuss our work on residential real estate valuations which encompass appraisals and other value estimation methods. My statement summarizes the report on residential appraisals we are releasing today which responds to a mandate in the Dodd-Frank Act.

Among other things, the report discusses: first, the use of different valuation methods and their advantages and disadvantages; and second, conflicts of interest in appraisal selection policies and views on the impacts of these policies on industry stakeholders and appraisal quality.

In summary, we found that appraisals are the most commonly used valuation method for first lien residential mortgage originations. While data on different appraisal approaches are limited, we found that the sales comparison approach is required by Fannie Mae, Freddie Mac, and FHA and is reportedly used in nearly all appraisals. We also found that the cost approach, in which an estimate of value uses data on land value and what it would cost to replace or reproduce a residence, is often used in conjunction with the sales comparison approach.

With respect to the second topic that I just raised on conflict of interest policies, including the Home Valuation Code of Conduct, these policies have changed appraisers' selection processes in the appraisal industry more broadly. Specifically, the policies have led to increased use of appraisal management companies, which are also called AMCs. Federal regulators and the Enterprises said they held lenders responsible for ensuring that AMC's policies and practices meet their requirements for appraiser selection, appraisal review, and reviewer qualifications, but that they generally do not directly examine AMC's operations. The Dodd-Frank Act places its supervision of AMCs with State appraiser licensing boards and requires the Federal banking regulators, the Federal Housing Finance Agency, and the Bureau of Consumer Financial Protection to establish minimum standards for States to apply in registering AMCs.

Setting minimum standards that address key functions AMCs perform on behalf of lenders would enhance oversight of appraisal services and provide greater assurance to lenders, the Enterprises, and others of the credibility and quality of the appraisals provided by AMCs. Therefore, we recommend that these regulators consider addressing several key areas, including criteria for selecting appraisers, as part of their joint rulemaking under the Act to set minimum standards for States to apply in registering AMCs.

Chairwoman Biggert and Ranking Member Gutierrez, this concludes my prepared statement. I would be happy to answer any questions.

[The prepared statement of Mr. Shear can be found on page 218 of the appendix.]

Chairwoman BIGGERT. Thank you, Mr. Shears.

Ms. Norton, you are recognized for 5 minutes.

STATEMENT OF ANNE BALCER NORTON, DEPUTY COMMISSIONER, MARYLAND OFFICE OF THE COMMISSIONER OF FINANCIAL REGULATION, ON BEHALF OF THE CONFERENCE OF STATE BANK SUPERVISORS

Ms. NORTON. Thank you. Good afternoon, Chairwoman Biggert, Ranking Member Gutierrez, and distinguished members of the subcommittee. My name is Anne Balcer Norton, and I serve as the Deputy Commissioner of the Office of Financial Regulation for the State of Maryland. It is my pleasure to testify before you today on behalf of the Conference of State Bank Supervisors. I would also like to recognize Maryland's Secretary of Labor, Licensing and Regulation, Alex Sanchez, who is here with me today.

I thank you for holding this hearing on issues affecting residential mortgage origination. State regulators play a central role in overseeing mortgage origination markets, and we appreciate the opportunity to be part of this important discussion.

My statement today will touch briefly on changes and improvements to State mortgage regulation. The policy and regulatory response to the financial crisis remains a work in progress, involving Congress as well as State and Federal regulators. State mortgage regulators have been focused on improving and enhancing mortgage regulation to better protect the consumer and to strengthen the mortgage market itself. Key to these goals is ensuring that the industry is diverse and supports a variety of business models.

The Nationwide Mortgage Licensing System and Registry, or the NMLS, was conceptualized and created by State regulators to unify State mortgage supervision in a single framework. NMLS provides the foundation for coordinated, consistent, and comprehensive supervision of the mortgage industry.

At its launch, NMLS was a voluntary State initiative. Subsequently Congress, through the leadership of Chairman Bachus, embraced and codified NMLS into Federal law through the SAFE Act, creating an integrated and comprehensive State-Federal approach to mortgage supervision.

State regulators have moved aggressively to implement the many provisions of the SAFE Act, which include providing free consumer access to licensing information and creating a mortgage call report. Just 3 years after the passage of the SAFE Act, nearly every single residential mortgage loan originated in this Nation will be performed by a loan originator who is either State licensed or federally registered through NMLS.

NMLS and the SAFE Act are key parts of a larger effort aimed at creating a framework for seamless and comprehensive mortgage origination, but this framework still relies on regulators to supervise the industry effectively.

In 2008, CSBS and AARMR established the Multi-State Mortgage Committee, or the MMC, to serve as the coordinating body for examination and enforcement supervision of multi-State mortgage entities by State mortgage regulators. Innovative examination techniques and sophisticated software utilized by the MMC have radically improved supervision of the residential mortgage industry and have uncovered fraudulent behavior in some mortgage companies. As a result of these examinations, State regulators have been forced to take enforcement actions when fraud is found, which in some cases has resulted in revocation of licensure. Just last month, the MMC coordinated a multi-State settlement with the Mortgage Access Corporation after an examination found numerous compliance and internal control deficiencies.

With regard to the climate in the mortgage industry and the other areas that we supervise, State regulators see a great deal of anxiety that reflects fears about the effect of the Dodd-Frank Act and other regulatory actions deemed necessary to address identified weaknesses in the financial system.

For instance, the Federal Reserve's loan originator compensation restrictions have presented challenges in terms of implementation. State regulators support the prohibition of payments to mortgage brokers or loan officers based on a loan's interest rate or payment features, but are struggling to provide field examiners with clear guidance on how to evaluate industry compliance. Official guidance from either the Federal Reserve or the CFPB is needed to provide directions to regulators and clarity for the industry.

As in other areas of financial services, State financial regulators remain concerned about policies that encourage or accelerate industry consolidation. The challenge for policymakers and the regulators who implement these policies is to create a regulatory framework that ensures industry professionalism and accountability. We must also ensure there are no unnecessary regulatory inefficiencies and burdens for State regulators. Policies and approaches that encourage regulatory collaboration and coordination and that support regulatory innovation have been vital to striking this balance.

Thank you for the opportunity to testify before you today. I look forward to answering any questions that you have.

[The prepared statement of Ms. Norton can be found on page 147 of the appendix.]

Chairwoman BIGGERT. Thank you, Ms. Norton.

We will now move to questions, and each member will have the opportunity to ask questions for 5 minutes, and I will recognize myself for 5 minutes. I would address this to Ms. Payne.

Looking at the underlying law, and I have looked at that several times, but nowhere do I see reference to modest referral payments on homeowner warranties as one of the objectionable practices that Congress sought to outlaw in 1982. Would you agree that Congress did not explicitly cover homeowner warranties in the text of RESPA?

Ms. PAYNE. Thank you for the opportunity to comment on that question.

From HUD's perspective, the statutory language prohibits referral fees amongst settlement service providers and the statutory language also identifies several types of settlement service providers, and it is not an exhaustive list, as was determined in 1992 when HUD's regulations determined that it did cover home warranty companies.

Chairwoman BIGGERT. While I appreciate your suggestion in your written testimony that Congress should first study the issue, I will ask if HUD studied this issue first before issuing its rule and guidance?

Ms. PAYNE. Thank you for that question. The guidance in 1992, was that your question?

Chairwoman BIGGERT. 1982 and 1992.

Ms. PAYNE. I don't know off the top of my head the regulatory history behind what was studied prior to enacting, but I will be happy to go back and do some research and get back to you on that question.

Chairwoman BIGGERT. Okay. It seems that for over 20 years, HUD has allowed home warranties to be sold through real estate agents and brokers under RESPA, and yet the new interpretation by HUD in recent years has cited this practice as a RESPA violation and created an incentive for litigation.

Could you explain HUD's rationale for prohibiting the home warranty sales through the real estate agents and brokers?

Ms. PAYNE. Yes. Thank you for that question.

HUD's interpretation was simply a clarification of its long-standing opinion on this.

Chairwoman BIGGERT. Has there been any evidence that consumers have been harmed?

Ms. PAYNE. The harm to consumers on the underlying policy would be beyond the scope of RESPA as RESPA reads today on the underlying warranty. However, I can tell you that, just to go back to your previous question if I may, HUD did simply reiterate HUD's long-standing policy that a real estate broker or agent must perform actual, necessary, and distinct services from their primary services for which there are not duplicative fees. And the rationale in HUD's longstanding interpretation has been that referral fees tend to unnecessarily increase closing costs for consumers because those costs are ultimately borne by the consumer.

Chairwoman BIGGERT. Even though it was done for 20 years. Thanks.

Now, I will turn to Ms. Braunstein. The appraisers independence provision of the Dodd-Frank Act, section 1472, requires lenders to compensate fee appraisers at a rate that is "customary and reasonable" and the Fed has issued related rules. Should the government be in the fee setting business?

Ms. BRAUNSTEIN. Actually, in determining what is customary and reasonable, we precisely did not set fees. We talked about a process by which someone could arrive at a fee that would be considered customary and reasonable, but we did not publish fee schedules or set specific prices. Part of the reason for that is that it would be very difficult to do that, given all the factors that need to be taken into account in determining the fee.

Chairwoman BIGGERT. Do you think this provision in Dodd-Frank should be repealed, or do you think it is a good provision? How are people going to know what is reasonable and customary?

Ms. BRAUNSTEIN. What we tried to lay out was a means by which you could arrive at those conclusions by looking at the scope of the work, the qualifications of the appraiser, and what the customary rates are in the geography where it is taking place. There are methods to do that. There also was an alternative provided that was in the statute whereby companies could rely on surveys that are done in local markets. So, there are a number of ways to determine that.

Chairwoman BIGGERT. Okay. Thank you. My time has expired.

Mr. Gutierrez, you are recognized for 5 minutes.

Mr. GUTIERREZ. Thank you so much. First, I would like to ask Ms. Braunstein, could you just tell us three significant consumer protection actions that have been taken in the last 3 years, the 3 most significant ones that come to your mind?

Ms. BRAUNSTEIN. By the Federal Reserve, you mean?

Mr. GUTIERREZ. Yes, by the Federal Reserve under your leadership.

Ms. BRAUNSTEIN. Yes. I think enacting the HOEPA rules over high-cost mortgages and putting those protections in place was significant. I also think putting the prohibitions on loan originator compensation was significant. It is hard to say. I think some of the things that are being done in requiring ability to repay throughout the entire market, which is somewhat a codification of what we did in HOEPA, but for a larger population of loans, I think that is also quite significant.

Mr. GUTIERREZ. That is, you have to take into consideration the ability to repay?

Ms. BRAUNSTEIN. The ability to repay the loan, yes.

Mr. GUTIERREZ. Because many loans were—

Ms. BRAUNSTEIN. They were made without taking those considerations—frankly, without doing good underwriting.

Mr. GUTIERREZ. Good underwriting, like—

Ms. BRAUNSTEIN. Income.

Mr. GUTIERREZ. It is 5 percent today, 7 percent next year, maybe 11 or 12 percent in years and you can't make the payment. It looks good the first year, but maybe the second, the third and the fourth you can't make the payment. Those are cases you probably see, not exactly in those.

Ms. BRAUNSTEIN. You are talking about teaser rates.

Mr. GUTIERREZ. Without any relationship to my income or possible income into the future.

Ms. BRAUNSTEIN. Correct.

Mr. GUTIERREZ. I think those are significant. How long did it take to put—when did you first begin to put the HOEPA rules in place?

Ms. BRAUNSTEIN. We held hearings in 2007 and we released the final rules in 2008.

Mr. GUTIERREZ. In 2008. And were there practices that have been—have you outlawed practices that have been longstanding practices?

Ms. BRAUNSTEIN. Yes. We addressed problems that we identified in the mortgage market, some of which I would say were more longstanding than others, some of which came about as a result of the subprime boom in the market and were specifically identified.

Mr. GUTIERREZ. Some might be more recent rules necessary given the new generation of products.

Ms. BRAUNSTEIN. Right. We looked at the markets at that time, the products that existed, where there were problems.

Mr. GUTIERREZ. But if something were going on for 10, 15, or 20 years, you wouldn't say it has been going on for 10, 15, or 20 years, so we shouldn't take a look at it.

Ms. BRAUNSTEIN. If it is causing a problem in the marketplace, and in particular it is causing a problem and concern for consumer protection, we should address it regardless of how long it has been going on.

Mr. GUTIERREZ. Excuse my ignorance, but I have enjoyed having you testify before us for so many years. Are you staying at the Federal Reserve?

Ms. BRAUNSTEIN. Yes, I am.

Mr. GUTIERREZ. Ms. Payne, you are going over to the new Consumer Protection Agency?

Ms. PAYNE. Yes, sir.

Mr. GUTIERREZ. And when do you start there?

Ms. PAYNE. July 31st.

Mr. GUTIERREZ. July 31st. Who are you going to report to when you get there?

Ms. PAYNE. I am going to be reporting to the enforcement office under Mr. Richard Cordray.

Mr. GUTIERREZ. And does he have a boss?

Ms. PAYNE. I assume so. Maybe an acting boss.

Mr. GUTIERREZ. An acting boss. Do you think you might be reporting to someone who will be reporting to an acting person?

Ms. PAYNE. I am not sure what the structure will be. I am not that familiar at this point, and I can't speak on behalf of the CFPB.

Mr. GUTIERREZ. You can't speak on their behalf. Right. I still have time. Thank you. We get along so well, we chat sometimes up here just by ourselves.

I am looking forward to you going over there, and—

Ms. PAYNE. Thank you.

Mr. GUTIERREZ. —putting that agency together. Because I think one of the things fundamental to a democracy is if a majority of legislators in the House and a majority of legislators in the Senate get together, go to conference, a public conference, the kind of public conference I haven't seen since I have been here in 18 years; that is, we spent days and nights in public and we came up with a product and that product has certain people in charge of certain agencies and directors in charge, I just find it a little undemocratic to then one year later say, forget all that process, unless, of course you go through a process that undoes all of that. Right?

So I kind of just want to use these moments to say that I hope that there won't be those who will use undemocratic approaches, approaches that aren't transparent and clear, to thwart a majority that has been elected by the American people and signed by the

President of the United States, so that you might have real supervisory personnel when you get there, just like you have at HUD.

Thank you so much for your testimony today.

Chairwoman BIGGERT. Thank you.

Mr. Hurt, you are recognized for 5 minutes.

Mr. HURT. Thank you, Madam Chairwoman. Thank you all for appearing before us today. I had a question for Ms. Braunstein and maybe sort of a follow-up with Ms. Cochran.

On April 1st, the Fed issued a final rule governing loan originator compensation, and there have been some complaints about the vagueness of that final rule. I was wondering, does the Federal Reserve Board intend to issue formal guidance, and if so, why, and if not, why not?

Ms. BRAUNSTEIN. When the Federal Reserve Board issued the rules last year in 2010, we did issue guidance in the form of an official staff commentary on that rule. Since then, we have also answered numerous questions and inquiries about that rule. We have provided a lot of guidance to industry. And in fact, we held a webinar just a few months ago where we had over 19,000 people listening in on that. And when people have asked us for clarifications, we have provided those clarifications.

Mr. HURT. But that is not the same as formal guidance, is it?

Ms. BRAUNSTEIN. In terms of formal guidance, the official staff commentary is formal guidance.

Mr. HURT. This is to Ms. Cochran. Ms. Cochran, do you know whether or not the CFPB intends to review this final rule because of the jurisdiction that you all will be given over consumer financial products and services?

Ms. COCHRAN. Under Title XIV of the Dodd-Frank Act, there is one additional issue with regard to loan originator compensation in situations where consumers have paid up-front discount fees. We know we need to go back and look at that issue because it is not addressed in the current rule. So, at a minimum, we will have that process and expect a notice and comment rulemaking.

Mr. HURT. And when will that transition take place?

Ms. COCHRAN. We are still planning out our process for the coming months. The regulation is due under the statute by January 2013, but we don't have a specific target date yet on the proposal. We are still planning that.

Mr. HURT. Ms. Payne, for you, I recently read a survey that was prepared relating to the RESPA reform that suggested that 56 percent of the buyers said they did no comparison shopping among lenders at a time when HUD's focus on consumer shopping seemed to be at the top of the list. Additionally, 49 percent of the buyers said that good faith estimate disclosure was too complicated, a waste of time, or they weren't sure.

I was wondering if you could comment on the suggestion that perhaps this RESPA reform is not headed in the direction that you all obviously would like it to be?

Ms. PAYNE. Thank you for that question. I can take it in a few parts.

We spent the better part of a year working on educating and bringing everybody into compliance. The way I looked at the new RESPA rule, I would describe it that it really changed the culture around the GSE forms and the settlement forms. So, we spent a lot of time internally working on education and implementation.

Mr. HURT. You mean culture within the agency?

Ms. PAYNE. Culture within the marketplace.

Mr. HURT. Or among consumers?

Ms. PAYNE. Among the consumers and the industry preparing the forms.

Your point about little or not enough comparison shopping by consumers, we also—as I said in my opening comments, I don't know if you were here—produced three consumer education videos to try to get consumers aware of the new culture and to help them shop. The three videos were "Shopping For Your Home"—

Mr. HURT. I heard you say that.

Ms. PAYNE. —"Shopping For Your Loan" and "Closing the Deal."

Mr. HURT. Who is watching them? How do you get them out there? On your Web site?

Ms. PAYNE. On our Web site. They are on HUD's YouTube channel.

Mr. HURT. You are hopeful that the videos will encourage a new culture among consumers to comparison shop?

Ms. PAYNE. We tried to get the word out through the National Association of REALTORS® to actually get them to show the videos to consumers when they come in there to try to purchase a home.

And as far as the GSEs, your comment about being too complicated, I think the RESPA rule has taken a good first step to change this culture. As you know, in a week we pass that baton to the CFPB and they have already started their process to further the RESPA–TILA reform efforts.

Mr. HURT. Thank you.

Chairwoman BIGGERT. The gentleman from Ohio, Mr. Stivers, is recognized.

Mr. STIVERS. Thank you, Madam Chairwoman. I appreciate everybody being here today and appreciate your time and all of your testimony.

I wanted to sort of talk about the QRM a little bit. What is going to be the role of the QRM with regard to, will it change the market share or the role of FHA versus the GSEs? Does anybody have a thought regarding that?

No one? Okay.

Does anybody have concerns about the ability-to-repay provision contained in Dodd-Frank and how it has been interpreted in the Qualified Residential Mortgage debate?

Ms. NORTON. Sir, I can jump in, particularly back to your original question relating to the FHA and GSE loans. What we are seeing on the State level, and particularly with the mortgage lenders that we supervise, that is the majority of their market and those are loans that are exempt under the new rules. So there is still, as I said in my testimony, a lot of uncertainty about how these are going to play out in practice.

The position of State bank regulators is that the QRM should be the best product on the market, but not the only product on the market. We agree with the rule's threshold and think it is necessary to have high standards. It is not the only product, but we also believe there needs to be a certain degree of flexibility, so as we start to see the market improve and additional products and participants in the market, that there is flexibility to adjust, to revisit, and to ensure that it is not stifling growth.

Mr. STIVERS. Great. With that in mind, Ms. Norton, do you have any concern that the definition of the Qualified Residential Mortgage is so tight that it is going to cause some problems in the marketplace?

Ms. NORTON. I think that is a good question. From our licensees, we hear concerns. Frequently, we are on the ground, and we hear quite a bit of feedback. But, again, from our perspective, it is still unknown. I think that is the unfortunate reason for my giving you what is probably not the best answer in that we don't know. And we see the market as concentrated right now with FHA and Fannie products, which are exempt, and our prediction is that this is not going to be the only product on the market, which we have tried to reassure our licensees. However, again, we don't know, which is why we hope to continue to work with our partners at the Federal level when we need to revisit any rules, not limited to this, to ensure that there is flexibility and it does not stifle growth.

Mr. STIVERS. Thank you.

Ms. Payne, with regard to your role at HUD, do you see significant barriers to private capital reentering the mortgage lending and secondary markets, and if so, do you have any thoughts about how we can make it a more hospitable environment for private capital?

Ms. PAYNE. Thank you for that question. That is really beyond the scope of my authority at HUD and my office, but I would be happy to take that question back and try to get you an answer.

Mr. STIVERS. Okay. What has HUD done to look at the impact of the policies that have been undertaken as part of some of the rules and the changes in Dodd-Frank and what they mean to existing homeowners and future homeowners? Have you looked at those two groups of people and what the new regulations mean to them?

Ms. PAYNE. From HUD's perspective, we have really been focusing on implementing the new RESPA rule most recently, and the SAFE rule, which just became finalized, that final rule, and then also now in transitioning everything to the CFPB, so I do not think we have gone in depth into analyzing that.

Mr. STIVERS. Thank you. I yield back.

Chairwoman BIGGERT. Thank you. We are happy to be joined again by the gentleman from Texas, Mr. Green. You are recognized for 5 minutes.

Mr. GREEN. Thank you, Madam Chairwoman, and I thank the ranking member as well. I am honored to have the opportunity to sit. I am not a part of the subcommittee, but thank you for allowing me to be an interloper.

Chairwoman BIGGERT. Yes, but you have the best attendance record.

Mr. GREEN. Thank you. With reference to the QRM, I talk quite a bit to constituents, many of whom are REALTORS®, and they talk quite a bit to people who purchase property. It all makes sense so far. They tell me that many of the consumers are concerned about 20 percent, that 20 percent is a bit much. I absolutely believe that zero is a bit too little for a QRM. The question becomes, is there someplace between 0 and 20 percent that is more appropriate? I understand that we have the 5 percent retention that is going to apply to these other products. Who would like to give me some intelligence on this in terms of how you are proceeding?

Thank you very much. It is very difficult for me to see names across, and I am confident I could look at the list, but if you would, please, ma'am?

Ms. BRAUNSTEIN. The Federal Reserve was involved with drafting the QRM rules. The first thing I would say is that the QRM is out for comment. We are getting a lot of comment on this proposal, and intentionally extended the comment period so that we could hear all the views before we move forward to produce final rules. In terms of your question about the criteria that are used, one thing to remember is that the QRM was intended to be a very narrow slice of the market, and that most housing loans would be outside the QRM, and that there would still be a robust market outside of the QRM.

Mr. GREEN. So far—and obviously we are not far enough along to have enough empirical evidence to give us a great assessment, but are you finding thus far that we are having these other products come to fruition? I am not hearing a lot about them, and I do not follow it as closely as you do, but what about the other products?

Ms. BRAUNSTEIN. At this point in time, as we all know, the housing markets are depressed, so there is not a lot of activity there, but I think envisioning a marketplace that recovers and is more robust, we would envision the QRM as being a narrower slice of that marketplace.

Mr. GREEN. Is it possible that a QRM, as presently constructed—and by the way, I supported Dodd-Frank, and I am really—this is a search for truth about this that I am engaged in. I do not want it to appear to be a quick-sided quest. Do you think that this, at this moment in time, may need some adjustment because we understand the importance of the role of the housing market in our recovery?

Ms. BRAUNSTEIN. The rules have not taken effect. They are just proposed, and that is why we have the comment period, because we want to get the comments and make some determinations.

Mr. GREEN. Exactly. So the possibility still looms that it may be less than 20 percent?

Ms. BRAUNSTEIN. I have no idea what the final rules will show. We will look at the comments and then see. But the other thing to remember, obviously, is that we just came through a very difficult period where housing was a big problem and that one of the things this was intended to address is that people were saying there was not enough skin in the game.

Mr. GREEN. I understand. Because my time is limited, let me ask one additional question on this, and I may get in another.

With reference to the rule itself, when do you anticipate getting the final rule?

Ms. BRAUNSTEIN. I have no idea on that. It is an interagency process. We extended the comment period until August, and we have, I think, thousands of comments, so we will have to see after that.

Mr. GREEN. Let me quickly ask this question: On the 21st of July, rulemaking authority for RESPA will be transferred over to the CFPB. At that point, how will persons desiring to tweak certain rules have to go about it? I do not want you to give me all of the details, but do they then come before the CFPB or is HUD completely out of the picture? How does that work at that point?

Ms. COCHRAN. With regard to the rulemaking authority, that is correct, that on the 21st it transfers to the CFPB, and so if someone was interested in petitioning for a rulemaking, they would address the petition to the Bureau at that time.

Mr. GREEN. So, these questions concerning home warranties would then fall under the auspices of the CFPB on the 21st?

Ms. COCHRAN. That is correct.

Mr. GREEN. Thank you, Madam Chairwoman, for the time.

Chairwoman BIGGERT. Thank you, Mr. Green. I have just two questions, and then if there are no other questions, we can move to the next panel, since it is quite large.

Mr. Park, Congress established a funding mechanism and directed the Appraisal Foundation to do two things, standards and qualifications. Appraisal practices seemed to be outside of this area. Where do you see the role of the new Appraisal Practices Board fitting into the two mandates given by Congress?

Mr. PARK. The Appraisal Subcommittee is charged with overseeing the appraisal, with monitoring the Appraisal Foundation, and reviewing the Appraisal Foundation, particularly with respect to the Appraisal Standards Board and the Appraiser Qualifications Board. The subcommittee also provides a Federal grant to the foundation to carry out the activities of the standards board and the qualifications board. The practices board is not something that was—it is not part of Title XI, the foundation has done that of their own volition. We do monitor the practices board as part of our role, but that is the limit of it.

Chairwoman BIGGERT. Can the Appraisal Subcommittee direct the Appraisal Foundation to take certain actions then?

Mr. PARK. No. The Appraisal Foundation is a private organization, and the subcommittee has no authority to direct the Appraisal Foundation.

Chairwoman BIGGERT. So it is just monitoring and reviewing?

Mr. PARK. Yes, ma'am.

Chairwoman BIGGERT. Okay. What role did the Appraisal Subcommittee play in the creation of the Appraisal Practice Board?

Mr. PARK. The Appraisal Subcommittee played no role in the creation of the practices board.

Chairwoman BIGGERT. Okay. Thank you. And then Mr. Shear, is appraisal oversight sufficient as it is established now?

Mr. SHEAR. That is a question I cannot answer at this time, but one thing that I would like to mention is we have an ongoing audit that is mandated by Dodd-Frank. The due date on that is in January of 2012. We have interacted a lot with Jim Park and others associated with the Appraisal Subcommittee, and we are addressing many of the issues that are in Dodd-Frank, including funding type questions. So we are looking into it, and we will continue to interact with committee staff on it.

Chairwoman BIGGERT. Great, thank you. I would like to thank this panel so much for being here, and we appreciate all your testimony.

The Chair notes that some members may have additional questions for this panel which they may wish to submit in writing. Without objection, the hearing record will remain open for 30 days for members to submit written questions to these witnesses and to place their responses in the record.

Thank you so much.

If the panel will take their seats so that we can begin the second panel. I am glad to see that all the witnesses fit—almost. Thank you all.

With that, I will introduce the second panel: Mr. Steve Brown, executive vice president of Crye-Leike, on behalf of the National Association of REALTORS®; Mr. Henry Cunningham, CMB, president, Cunningham & Company, on behalf of the Mortgage Bankers Association; Mr. Tim Wilson, president, Affiliated Businesses, Long & Foster Companies, on behalf of the Real Estate Services Providers Council; Ms. Anne Anastasi, president of Genesis Abstract and president, American Land Title Association; Mr. Mike Anderson, president, Essential Mortgage, on behalf of the National Association of Mortgage Brokers; Mr. Marc Savitt, president, The Mortgage Center, on behalf of the National Association of Independent Housing Professionals; Ms. Sara Stephens, president-elect, Appraisal Institute; Mr. Don Kelly, executive director, Real Estate Valuation Advocacy Association, on behalf of REVAA and the Coalition to Facilitate Appraisal Integrity Reform; Ms. Janis Bowdler, director of the Wealth-Building Policy Project, Office of Research, Advocacy, and Legislation, on behalf of the National Council of La Raza; and Mr. Ira Rheingold, executive director, National Association of Consumer Advocates.

With that, let me just say that without objection, your written statements will be made a part of the record, and you will each be recognized for a 5-minute summary of your testimony. We will start with Mr. Brown. You are recognized for 5 minutes.

STATEMENT OF STEVE A. BROWN, EXECUTIVE VICE PRESIDENT, CRYE-LEIKE REALTORS®, ON BEHALF OF THE NATIONAL ASSOCIATION OF REALTORS®

Mr. BROWN. Madam Chairwoman, Ranking Member Gutierrez, and members of the subcommittee, I am Steve Brown, executive vice president and a 37-year practitioner in the real estate business based in Memphis, Tennessee. I thank you for the opportunity to testify on behalf of the 1.1 million members of the National Association of REALTORS® (NAR).

Crye-Leike is the Nation's sixth largest brokerage company, with a network of more than 3,600 licensed sales associates, 600 staff members, and over 130 offices located throughout Alabama, Arkansas, Florida, Georgia, Kentucky, Mississippi, Oklahoma, and Tennessee. In my testimony today, I would like to cover several issues affecting housing and the mortgage origination process.

A major issue facing real estate firms, home warranty companies, and consumers is the treatment of home warranties under the Real Estate Settlement Procedures Act, or RESPA. RESPA was enacted to prevent kickbacks for referrals among settlement service providers. Settlement service is defined as a service required to originate a federally-related mortgage. Traditional settlement service providers include lenders, real estate agents and brokers, title agents and companies, appraisers, and attorneys.

A home warranty is a contract issued to cover any needed future repairs for a list of specific appliances or systems spelled out in a warranty contract. Home warranties are a purely optional insurance product regulated by State law. Today, many times they aren't even purchased by buyers. Rather, sellers offer them as a way to facilitate a sale or they are sold after closing. Since many warranty companies do not employ a sales force, real estate firms and agents have been the industry's traditional means of making consumers aware of the product. For their processing, marketing, administrative, and after-sale problem-solving services, the real estate professional receives a modest stipend.

Despite the fact that a home warranty is not a required service to obtain a mortgage or buy a home, HUD long ago included home warranties in the list of settlement services subject to RESPA. This was not problematic since compensation to agents and brokers was considered appropriate under RESPA's long-standing exception that says a person can be paid for services actually performed. That changed when HUD issued a letter in 2008 that said the sale of warranties by real estate agents was essentially a per se violation of RESPA.

Since 2008, NAR has worked with HUD to obtain clarification and reverse this incorrect opinion. In 2010, HUD finally issued additional guidance. Unfortunately, that guidance has been even more problematic and has led to even more crippling class action lawsuits that are hurting the industry. Perhaps even more unfortunately, the guidance will likely make warranties more expensive and less easily available to consumers.

For these and other reasons, NAR urges the subcommittee to pass H.R. 2446, introduced by Representatives Biggert and Clay, to clarify that home warranties are not subject to RESPA while still providing for appropriate consumer disclosure.

Another area of concern is a problem that arises as a result of the definition of points and fees contained in the Qualified Mortgage provision of Dodd-Frank. The definition is complicated, but the effect is that mortgage companies with affiliates, such as the real estate firm's title company, in the transaction, must count affiliate charges toward a 3 percent cap on fees and points. A mortgage company without affiliates does not have to do so. As a result, many affiliated companies will not be able to offer a full array of services to their clients because in doing so they would violate the 3 percent cap.

The House addressed this issue in its version of the Dodd-Frank bill with an amendment by Representative Clay, which was removed during conference. Congress should rectify the 3 percent cap issue at its earliest opportunity so consumers can fully benefit from greater competition between affiliated and unaffiliated lenders.

Finally, I would also like to reiterate the importance of the FHA program to the Nation's real estate recovery. With credit already tight, FHA plays a vital role in providing affordable, well underwritten mortgage credit to American families. FHA's book of business since 2009 is performing extremely well. Pending changes to the FHA loan limit formula will result in significant declines in the current loan limits in 669 counties in 42 States. In my firm's market, FHA is used by more than 60 percent of our buyers. These declines will have a dramatic impact on liquidity in our markets and across the country. With housing markets struggling to recover, the last thing we need to do is put an avoidable stumbling block in the path of a much-needed housing recovery. I know it has been said before, but I believe it bears repeating: without a housing recovery, the Nation's economy as a whole will struggle to recover its balance.

I strongly urge the subcommittee to approve H.R. 1754, the Preserving Equal Access to Mortgage Finance Programs Act. This bill, introduced by Representatives Gary Miller and Brad Sherman, will make the current limits through FHA permanent and ensure that families across the country have ongoing access to affordable mortgages.

NAR opposed risky lending in 2004 when it approved the policy that called for strong mortgage underwriting. We now feel the pendulum has swung too far and fewer otherwise qualified people are able to get a loan. Congress and the Administration need to reexamine the impact of well-meaning laws and regulations that have come out of the financial mortgage crisis to ensure the still fragile housing and economic recovery stay on track.

I thank you for your attention.

[The prepared statement of Mr. Brown can be found on page 106 of the appendix.]

Chairwoman BIGGERT. Thank you so much.

Mr. Cunningham, you are recognized for 5 minutes.

STATEMENT OF HENRY V. CUNNINGHAM, JR., CMB, PRESIDENT, CUNNINGHAM & COMPANY, ON BEHALF OF THE MORTGAGE BANKERS ASSOCIATION

Mr. CUNNINGHAM. Thank you, Chairwoman Biggert, Ranking Member Gutierrez, and members of the subcommittee. My testimony today on behalf of the Mortgage Bankers Association comes at a time of great change in our industry. The recent economic crisis has led many lenders to alter their practices and return to a more traditional way of originating mortgages. As an independent mortgage banker operating in North Carolina, I can tell you firsthand that these changes are having a profound effect on our industry, consumers' access to credit, and our overall economy.

Back in April, I testified before the Capital Markets Subcommittee on the proposed risk retention rule. That rule and the Qualified Residential Mortgage definition continue to be MBA's top focus. Simply put, the rule proposed by the regulators would make credit more expensive and less available, especially for minority, low- to moderate-income, and first-time home buyers with little impact on reducing defaults. It is a rule that needs to be pulled back and resubmitted.

There is a parallel regulatory effort that I fear could be just as harmful to consumers and lenders. The Federal Reserve has proposed new rules implementing Dodd-Frank's ability to repay provisions. These rules would prohibit lenders from making mortgages unless they make a reasonable determination that the consumer has the ability to repay the loan. Dodd-Frank allows lenders to meet this requirement by originating a Qualified Mortgage, or QM.

Our concern is the rule offers a rebuttable presumption as an alternative to a true safe harbor. In order for the QM to work, lenders need an ironclad safe harbor, with brightline standards that can be easily proven. If the standard is uncertain, lenders will act more conservatively. If, however, there is a strong safe harbor, borrowers will enjoy greater access to credit and lower cost.

MBA believes the QM and QRM need to be harmonized. Both were designed by Congress to achieve the same purpose of achieving better, more sustainable lending. Regulators should strive to achieve definitions that are essentially the same. Because the QRM, as proposed, would exclude too many borrowers from the most affordable loans, MBA believes the QM proposal is a much better starting point for both sets of rules.

Another issue of importance is the ongoing implementation of the SAFE Act. This is a well-intended law but has placed considerable stress on States regulating lenders who operate in multiple States or who would like to hire registered loan originators working for federally-regulated lenders. Both problems could be resolved if the States adopted transitional licensing so that out-of-State or federally-registered originators could work for a period of time as they qualify for State licensing. Furthermore, we strongly oppose States covering servicers under the definition of loan originators. This is something Congress never intended.

We also call your attention to the difficulties we have had with the recent loan officer compensation restrictions from the Federal Reserve. The rule was finalized with too little guidance and has led to great confusion. We urge the CFPB, which will take over TILA responsibility, to review this rule and listen closely to the concerns of the industry before it moves to implement similar provisions under Dodd-Frank.

Finally, MBA is grateful to see RESPA and TILA finally come under one roof. We hope the CFPB also draws on the expertise of the housing industry as it merges these two disclosures. Lenders work with consumers every day and have extensive experience conveying information to consumers in the most useful manner.

Madam Chairwoman, I am concerned that this wave of regulation, while well intended, will further tighten credit and smother a fragile housing recovery. Cunningham & Company is not a big lender. We did not cause the housing crisis. Last year, we originated $440 million in mortgages, 97 percent of which were fixed-rate mortgages and prime fixed-rate mortgages. We have been in the business for 21 years and employ 88 people. We are certainly not too-big-to-fail, but sometimes I feel we may be too-small-to-comply.

I would urge this panel to continue providing strong oversight and act where necessary to ensure these new rules are being implemented in a manner that allows consumers to continue to enjoy the benefits of competition that smaller, independent firms like Cunningham & Company provide.

Thank you for the opportunity to testify today. I look forward to your questions.

[The prepared statement of Mr. Cunningham can be found on page 118 of the appendix.]

Chairwoman BIGGERT. Thank you very much.

Mr. Wilson, you are recognized for 5 minutes.

STATEMENT OF TIM WILSON, PRESIDENT, AFFILIATED BUSINESSES, LONG AND FOSTER COMPANIES, ON BEHALF OF THE REAL ESTATE SERVICES PROVIDERS COUNCIL, INC.

Mr. WILSON. Good afternoon, Chairwoman Biggert, and members of the subcommittee. My name is Tim Wilson, and I am president of the Affiliated Businesses for Long & Foster Companies and 2011 chairman of the Real Estate Services Providers Council, known as RESPRO®.

Long & Foster Companies is the third largest residential real estate brokerage firm in the Nation, with 13,000 real estate associates operating out of 185 offices in the 8-State Mid-Atlantic region. We offer a full array of mortgage, title, and insurance services through affiliated business arrangements that are regulated at the Federal level under RESPA.

Today, I am representing RESPRO®, a national nonprofit trade association of almost 200 residential real estate brokerage, mortgage, home building, title, and other companies that offer one-stop shopping for home buyers through affiliated businesses. Firms like Long & Foster use our affiliated companies to help assure that our real estate customers close on time and move into their new homes as scheduled. Because we own or partially own other companies needed to close the home purchase transaction, we can resolve any service issues more efficiently than independent companies could. Our affiliated businesses also help us reduce the cost of the entire mortgage transaction through shared facilities, management, technology, equipment, and marketing expenditures.

Long & Foster is not alone in offering one-stop shopping through affiliated businesses. According to the independent real estate research firm REAL Trends, the Nation's 500 largest residential real estate brokerage firms closed over 150,000 mortgage loans and conducted over 350,000 title closings through affiliated companies in 2010.

My testimony today will focus on how the Dodd-Frank ability to repay and risk retention standards discriminate against affiliated businesses in a way that will reduce competition and increase mortgage credit costs in many marketplaces throughout the country.

As you know, Dodd-Frank provided a rebuttable presumption that Qualified Mortgages, or QMs, comply with its ability to repay standards. It created a similar category of Qualified Residential Mortgages, or QRMs, under its risk retention standards. Dodd-Frank specified that a mortgage cannot be a QM if the total points and fees paid by the consumer in the transaction exceed 3 percent of the loan amount and that a QRM cannot be defined more broadly than a QM.

The problem for affiliated businesses is that Congress used a 1994 HOEPA points and fees definition that counts fees paid to a mortgage lender's affiliated company towards the 3 percent threshold, but not fees paid to an unaffiliated company. As a result, loans in which a mortgage lender's affiliated title company is used would more likely exceed the 3 percent threshold, which means that they would not qualify as QMs under the ability to repay test or as QRMs under the risk retention standards.

Since the consequences of not being a QM or QRM are severe, companies with affiliated mortgage and title businesses, like Long & Foster, would need to discontinue offering either mortgage or title services in conjunction with those loans in which a 3 percent threshold would be exceeded. Competition in many marketplaces in the country would decrease because of the withdrawal of affiliated businesses. This ultimately would increase the cost of mortgage credit for consumers. Because 3 percent is more easy to reach on smaller loans, the impact would be most predominant in low-income or lower- to middle-income marketplaces.

There is absolutely no reason to discriminate against affiliated mortgage lenders in this manner. The affiliated mortgage companies of Long & Foster and other RESPRO® members use underwriting standards that meet Dodd-Frank requirements and have equivalent or even lower default rates when compared to the rest of the industry. Economic studies over the years have shown that affiliated title businesses are competitive in cost, and consumer surveys show consistently that consumers who use the real estate brokerage firm's affiliated businesses have a more satisfactory home buying experience.

RESPRO® believes that Congress can prevent this negative impact on competition and mortgage credit costs by creating a narrow exemption for affiliated title fees from the 3 points and fees threshold. For reasons identified in my written statement, we believe this narrow exemption would correct the problem without being inconsistent with the goals of Dodd-Frank.

Thank you for the opportunity to testify, and I look forward to your questions.

[The prepared statement of Mr. Wilson can be found on page 247 of the appendix.]

Chairwoman BIGGERT. Thank you, Mr. Wilson.

Ms. Anastasi, you are recognized for 5 minutes.

STATEMENT OF ANNE ANASTASI, PRESIDENT, GENESIS ABSTRACT, LLC, AND PRESIDENT, AMERICAN LAND TITLE ASSOCIATION

Ms. ANASTASI. Madam Chairwoman, Ranking Member Gutierrez, and members of the subcommittee, I am Anne Anastasi, president of Genesis Abstract in Hatboro, Pennsylvania. For the past 33 years, I have worked as a land title professional, and I am the current president of the American Land Title Association (ALTA).

ALTA members serve as independent third-party facilitators who conduct real estate and mortgage closings. We interact with consumers every day at the closing table where we are responsible for two major functions: first, we ensure that the transaction is completed quickly, honestly, and in accordance with all of the parties' instructions; and second, we serve as the last resource for consumers if they have questions about the fees that they are paying or the documents they are signing at closing. These closings can often feel daunting because most consumers only experience a closing a few times in their lives. Because of our special view into the consumer's experience, ALTA supports improvement to the mortgage process, and our members can be especially useful to policymakers as they consider how best to accomplish this task.

As we seek to improve the mortgage origination process, we need to fundamentally rethink a key part of the architecture of the current process: the Federal mortgage disclosure laws. These laws are designed to help consumers shop for a mortgage and settlement services by reducing confusion and providing the consumer with timely information about their transaction. However, our experience with consumers at the settlement table reveals that a significant amount of confusion still exists. As efforts are undertaken to revise and combine the mortgage disclosures required under RESPA and TILA, we offer the following three recommendations to improve the process.

First, improve the disclosures transparency by itemizing all costs, not just some. ALTA members routinely see the confusion caused by the current practice of itemizing some fees while combining other fees into categories or roll-ups. In addition, the greater transparency provided by full itemization increases information to help consumers shop for settlement services among competing providers, promoting competition and reducing excessive fees.

Second, make disclosures flexible enough to be applicable in all parts of the country. While real estate closings and practices vary greatly from State to State, the 2010 RESPA regulation created a regime that forces transactions into a one-size-fits-all disclosure. In many parts of the country, a number of fees that must be listed on the borrower's GFE are actually paid by the seller. Despite this, the latest RESPA regulation includes strict rules that require that these fees be irrationally disclosed as the borrower's responsibility. While appropriate credits are given on other lines of the new proposed combined disclosure, this unnecessary confusion must be explained to consumers by the lender and the closing agent.

One example of this paradox is the owners' title insurance policy. In many parts of the country, owners' title insurance is paid for by the seller. However, the lender and closing agent must disclose this charge as a borrower's cost. Not only does this create confusion, but the consumer starts to question the integrity of the transaction when we have to sit at the closing table and say, we are showing this fee on your side of the ledger. Do not worry about it. We will give you a credit on some other page.

Our last recommendation is that if the purpose of the Federal mortgage disclosure is to protect consumers, then every effort should be made to ensure that the disclosure helps consumers make educated choices. At a minimum, these disclosures should not prejudice consumers against protecting themselves. The current draft of the initial disclosure form includes the term "not required" when they describe settlement services that are not for the lender's benefit.

One example is owner's title insurance which, if it is purchased, indemnifies consumers against challenges to the title to their property. If a consumer chooses not to purchase this coverage, their financial interests are not protected, even though the lender is protected by a loan title insurance policy. Disclosure forms should avoid prejudicial phrases like "not required" that could imply that a particular service is of less value to the consumers. We know, as a result of the robo-signing and the foreclosure crisis, that the purchasing of an owner's title insurance policy is a prudent decision.

We encourage the CFPB to find alternative terms when describing these types of services such as "additional protections" or "recommended." How can we say we want to protect consumers when an unfortunate choice of words could lead to a misinformed and dangerous decision with unintended consequences?

ALTA is eager to serve as a resource, and we welcome your questions. Thank you very much.

[The prepared statement of Ms. Anastasi can be found on page 55 of the appendix.]

Chairwoman BIGGERT. Thank you so much.

Mr. Anderson, you are recognized for 5 minutes.

STATEMENT OF MIKE ANDERSON, CRMS, VICE PRESIDENT & CHAIRMAN OF GOVERNMENT AFFAIRS, NATIONAL ASSOCIATION OF MORTGAGE BROKERS

Mr. ANDERSON. Good afternoon, Chairwoman Biggert, Ranking Member Gutierrez, and members of this committee. And thank you for inviting me to testify today.

For decades, this country has encouraged homeownership because we believe it is the bedrock of building strong communities. However, we find ourselves at a tipping point relative to homeownership. In this down economy, we are no longer encouraging people to climb that ladder. In fact, we are making it increasingly more difficult at every single turn. We are destroying the ladder of homeownership.

First-time home buyers will find it virtually impossible to purchase a home in most markets if a 20 percent downpayment rule is required. This will mean that the current homeowners looking to move up will find it more difficult to sell their home because of the shrinking pool of eligible home buyers. As a result, home values will continue to decline.

Since 2007, our industry has been overwhelmed by literally thousands of pages of legislation, regulation, and disclosures aimed at helping the consumer better understand the mortgage process. However, here we are today, 4 years later, and the outlook for our housing recovery is dismal at best. While homes are more affordable now, new regulations, extremely tight underwriting, high unemployment, and low consumer confidence are preventing would-be home buyers from entering the market.

The recent rule regarding loan originator compensation has created the most unlevel playing field I have seen in my 30 years in the business. It is so flawed and biased against the small businesses that we have little chance of competing with the large banks, thereby reducing consumer choice and competition in local communities. I receive emails every single day from small businesses closing their doors because of this rule.

I want to give you just a few examples. After I quote a consumer a mortgage rate and fees, I cannot lower my price to compete against the bank next door. You heard that right. I cannot lower my price to compete with the bank next door under any circumstances. Honestly speaking, you have to admit that this is just not right. If the consumer pays a broker commission, I cannot pay my loan officer who worked with that consumer a commission for that transaction.

Lastly, at the closing table, many consumers find themselves short a few hundred dollars with circumstances beyond their control. I cannot reduce my profit to help the consumer whatsoever. We all know in this room that this is wrong. And I would like to say, you will miss us when we are gone. We are urging Congress and the CFPB to amend LO comp.

Before I conclude, I also want to touch briefly on the subject of the QRM. I have with me a chart prepared by the Federal Reserve Bank that illustrates foreclosures by loan type from 1998 through 2007. Looking at the data outlined in the chart, it is clear what caused the mortgage crisis. It was bad loan products.

So what should we conclude from this? In short, if it is not broken, please do not try to keep fixing it. Fixed mortgages were not the culprits in the mortgage crisis. We need to slow down and consider the unintended consequences of this rule.

When the FDA discovers that a prescription drug is causing harmful side effects to consumers, it exercises its authority to pull the drug off the shelves. The agency does not seek to overhaul the way doctors prescribe all medication or how pharmacists fill those prescriptions. So we need to take the same approach.

I want to thank you for letting me testify today, and if there are any questions, I will be happy to answer them.

[The prepared statement of Mr. Anderson can be found on page 65 of the appendix.]

Chairwoman BIGGERT. Thank you so much, Mr. Anderson.

Mr. Savitt, you are recognized for 5 minutes.

STATEMENT OF MARC SAVITT, CRMS, PRESIDENT, THE NATIONAL ASSOCIATION OF INDEPENDENT HOUSING PROFESSIONALS

Mr. SAVITT. Good afternoon, Chairwoman Biggert, Ranking Member Gutierrez, and members of the committee. I am Marc Savitt, president of the National Association of Independent Housing Professionals (NAIHP). Thank you for inviting NAIHP to testify on these important issues which are critical to the restoration of our housing market and the overall economic health of our country.

NAIHP represents small business housing professionals in all 50 States and the District of Columbia. Our members are Main Street USA who assist consumers through the difficult maze of purchasing or refinancing residential real estate. For the past 4 years, two Administrations and Congress have sought a solution to reenergize the housing industry. Despite the most affordable home prices and lowest interest rates in a generation, tax credits and other incentives, our Nation's housing market continues to underperform.

Like so many of the housing professionals I represent, I am a small business owner. In today's market, I not only struggle to attract new business, I am also severely overburdened with an onslaught of punishing rules and regulations that are destroying small business, killing jobs, and harming consumers. Worst of all, there does not seem to be an end in sight.

Let me give you an example. Under the SAFE Act—which we supported, by the way—I was required to go through an extensive background investigation: fingerprinting; credit check; two written examinations, both the State and Federal; 20 hours of preeducation; and the purchase of a surety bond. However, despite having met these strict qualifications, I cannot be trusted to order a residential real estate appraisal.

To remind the committee, it was not mortgage brokers or originators who were the subject of former New York Attorney General Cuomo's investigation. It was the federally-chartered banks. Moreover, these same banks now enjoy additional profits from their joint venture relationships with unregulated appraisal management companies and have complete control over the valuation system in this country. Regulators and consumers justify excluding brokers from the appraisal process because they claim having a financial interest in the transaction is a conflict of interest. If this were really about conflicts of interest, then banks, who have already been implicated in appraiser coercion, would not be allowed to have joint venture relationships with the appraisal management companies and share profits. This is about market share.

The bank and AMC joint ventures have also led to the assassination of the appraisal industry. Under these guidelines, license appraisers have two choices: work for the AMCs for fees between 40 and 60 percent less than what is customary and reasonable in their geographic area; or go out of business. Many thousands of appraisers have gone out of business across the country. These guidelines have increased the costs for consumers by an estimated $2.8 billion a year. Is there a consumer benefit? Absolutely not. Since May 1, 2009, the day these guidelines were implemented, valuation fraud has increased over 50 percent. These guidelines have also contributed to the continuing decline in property values.

With your permission, Mrs. Biggert, I would like to take the remainder of my time to address some comments that were made by Ms. Braunstein from the Federal Reserve Board.

Chairwoman BIGGERT. Without objection, it is so ordered.

Mr. SAVITT. Thank you. She made some comments, first of all, saying they had a webinar on March the 17th, which they did, to try to explain and clarify what was involved with the loan officer compensation rule. It is our understanding that there were approximately 10,000 people on that call. A few days before that call, they came out with the slides, they issued the slides that they were using in their presentation, and every one of those slides had a disclaimer on it which basically said, "Do not hold us to this." So, there really was not much of a clarification. She mentioned a compliance guide. The compliance guide, which they submitted after they received a letter from the SBA's Office of Advocacy because they had not submitted one at first, they finally did submit one which amounted to a 4-page cut-and-paste out of their rule.

They have steadfastly refused to answer questions in writing. They will tell you anything you want to know verbally. They will not answer any questions in writing, which puts all of us in this industry in a position to be sued because we do not know what they want us to do. We have asked numerous times, and sometimes even verbally, we get different answers.

The SBA's Office of Advocacy also still has a problem, even though they did turn in that 4-page cut-and-paste, they still have a problem with that. They wanted a proper compliance guide because in the Fed's rule itself, it said there would be a significant economic impact on small entities, but the Fed, of course, never addressed that.

The last thing is, as you may know, NAIHP and NAMB filed suit against the Federal Reserve Board over this compensation rule, and in the answer to our lawsuit, the Federal Reserve Board acknowledged that there was no difference because, as you know, this was over the unfair and deceptive practice of what they were claiming Yield Spread Premiums or YSPs were, that they did acknowledge that there was no difference between broker YSP and what they called lender YSP or creditor YSP.

Thank you.

[The prepared statement of Mr. Savitt can be found on page 207 of the appendix.]

Chairwoman BIGGERT. Thank you.

Ms. Stephens, you are recognized for 5 minutes.

STATEMENT OF SARA W. STEPHENS, MAI, CRE, PRESIDENT-ELECT, APPRAISAL INSTITUTE

Ms. STEPHENS. I would like to thank the chairwoman, the ranking member, and the members of the subcommittee for the opportunity to be with you today.

Professional real estate appraisers are analysts of local markets. Their research and opinions help protect the safety and the soundness of our banking system and provide a tool that defends mortgage lenders. Today, many lenders enabled by government policies continue down a treacherous path toward the commoditization of appraisals, promoting collateral validation over collateral valuation. This puts banks, home buyers, and taxpayers at risk. Unfortunately, for many years, appraisal has been viewed as an impediment to closing deals. Like other risk management functions, appraisal has been marginalized with many financial institutions as evidenced by recent investigative reports which tell how loan production rules and financial institutions lack a risk chromosome. New policies intended to correct past regulatory failures have concentrated power over appraisal decisions in the hands of a few. Coercion of appraisers has taken on new forms, where some are proposing to dictate the outcome of appraisals by actually legislating how to conduct an appraisal. All of these actions serve to effectively tie the hands of appraisers. Strangely, real estate agents have reported that consumers are paying higher appraisal fees, yet fees actually paid to appraisers have declined, in some cases by more than 40 percent.

How can this be? Simply put, lenders have added administrative expenses onto the backs of the consumers through the appraisal line on the HUD–1 form. Further, many lenders have chosen to outsource the appraisal management function to third-party management companies who pass only a fraction to the appraiser actually performing the appraisal service. Current policy leaves consumers completely in the dark. Here, we need transparency between appraisal and appraisal management fees, especially since it is the consumer who pays these fees in nearly all transactions.

Given the diversity of real estate, appraisals cannot and should not be developed like a cookbook with a set of recipes that dictate how an appraisal is to be developed. The Appraisal Institute's 80 years of experience have taught us that a credible appraisal process does not lend itself to a step-by-step, by-the-numbers, how-to guidebook. Instead, what is required is that the practitioner is sufficiently trained to understand the process as appropriate to the specific assignment.

For many appraisal problems, there is more than one solution. Take the valuation of green properties, our appraisals in declining markets. These are complex issues that require some flexibility of approach. Rules of thumb do not work. Credibility requires rigorous research and analysis, as for every rule there may be an exception. It also requires expertise by those using an appraisal or establishing processes around it.

To this point, Federal agency policies have resulted in caps on appraisal fees and propped up a business model of third-party middlemen. Unfortunately, the Federal Reserve's interim final rule is not faithful to congressional intent. The Appraisal Institute thinks Congress' intent was right on target. We urge Congress to guide the regulators' aim, directing them to correct the interim final rule to promote credibility over speed and cost.

We must also look at the process under which appraisal policies are overseen and implemented. Congress directed and funded the Appraisal Foundation to perform two functions: developing uniform appraisal standards; and establishing minimal appraisal qualifications. Without direction from Congress, the foundation has created a new board with no clear purpose or boundaries. Congress authorized the Appraisal Subcommittee, the Federal oversight agency of our profession, to monitor and review the activities and structure of the Appraisal Foundation, but not to direct or overrule its activities and structure. The Appraisal Subcommittee may have exceeded its congressional authorization with respect to the creation of the new board.

Such potential regulatory overreach is a huge concern. At a minimum, the recent actions of the Appraisal Subcommittee and the Appraisal Foundation should be examined by Congress, and we urge this committee to bring clarity and accountability to the relationship between the Appraisal Subcommittee and the Appraisal Foundation where it does not exist today.

In conclusion, last year Congress passed the most significant legislative update of the appraisal regulatory structure in 2 decades. In our view, this was only a beginning. Moving forward, Congress must maintain an active role in oversight of appraisal regulators and build on these reforms to address ongoing weaknesses. We can ill afford to allow another 20 years to pass without a thorough audit of appraisal regulations. Consumers, lenders, and taxpayers deserve much better than what they have been given to date.

Thank you very much.

[The prepared statement of Ms. Stephens can be found on page 230 of the appendix.]

Chairwoman BIGGERT. Thank you.

Mr. Kelly, you are recognized for 5 minutes.

STATEMENT OF DONALD E. KELLY, EXECUTIVE DIRECTOR, REAL ESTATE VALUATION ADVOCACY ASSOCIATION (REVAA), ON BEHALF OF REVAA AND THE COALITION TO FACILITATE APPRAISAL INTEGRITY REFORM

Mr. KELLY. Madam Chairwoman, and members of the subcommittee, I appreciate the opportunity to testify today both for REVAA and for the FAIR Coalition. On a personal note, as a former staffer of what was then called the Banking Committee, it is my great pleasure to be back here with you today.

In summary, first, REVAA and FAIR members provide valuable services to financial institutions, appraisers, and consumers in the course of the residential real estate appraisal.

Second, REVAA and FAIR members are working proactively with both the Federal Government and the States to implement the registration and regulatory requirements for appraisal management companies contained in the Dodd-Frank Act.

Third, we encourage the Consumer Financial Protection Bureau to rely on the research and reasoning utilized by the Federal Reserve Board for payment of customary and reasonable appraisal fees.

To my first point, REVAA members produce real estate valuation products, including appraisals and broker price opinions and others. They have been responsible for advancements in technology that benefit mortgage investors, servicers, originators, and ultimately consumers. FAIR is a coalition of five of the Nation's largest appraisal management companies.

AMCs typically operate a regional or national network of employee-based appraisers, independent contractors, and companies for the completion of appraisal reports. AMCs act as a centralized appraisal source for mortgage lenders that operate on a wide geographic basis. AMCs work to match the assignment with a qualified local appraiser. The average appraiser contracted for an assignment by a major AMC has 15 years of experience and typically travels less than 13 miles on any given assignment. AMCs perform extensive administrative and quality control functions on behalf of both the appraiser and the lender to ensure delivery of a high quality appraisal report.

Contrary to what some have suggested, appraisers directly benefit from working with an AMC by having an advocate to ensure appraisal independence to make sure that no improper attempt is made to influence the appraisal process. Much of the appraisal fraud that contributed to our current crisis has been linked to such improper influence. In addition, AMCs provide significant value-added services to appraisers, such as quality control, marketing, billing processes, etc., that reduce the cost of back room and administrative tasks. AMCs help consumers by reducing the time required for appraisal delivery and improving the quality of appraisers with efficient and effective quality control systems.

To my second point, AMCs are subject to new regulatory requirements under the Dodd-Frank Act, including new minimum standards and a national registry. Prior to the passage of the Act, several States had begun the process of enacting laws to require the registration of AMCs and to establish minimum requirements. AMCs have been actively involved with the States from the inception of these regulatory laws and have long supported transparency and independence in the appraisal process. We believe that it is important to work toward consistency and uniformity in the State laws and regulations to ensure that AMCs can effectively implement the necessary compliance procedures to operate on a national basis. We believe the Appraisal Subcommittee and the relevant banking agencies should contribute to ensuring a consistent set of requirements in this regard.

Finally, the Dodd-Frank Act required that lenders and their agents, including AMCs, compensate appraisers at a customary and reasonable rate for appraisal services. REVAA and FAIR believe that the Federal Reserve Board acted appropriately and logically to implement the congressional intent to this provision. The Board has recognized that appraisal services are not one-size-fits-all, as my friend Sara has indicated, and it has created a compliance structure for the payment of customary and reasonable fees that reflects market reality and ensures that the appraisal costs borne by consumers will remain fair and competitive.

While the Board's interim final rule remains effective without further finalization, we are concerned that some may ask the new consumer bureau to reconsider the rule with the intention to mandate a higher level of compensation for appraisers, one above market rates. This would be unfortunate, as consumers would then be subjected to higher appraisal fees without gaining any additional service for that fee. We hope that the new bureau, for the benefit of the consumer, will maintain the payment structure established by the Board.

Thank you for the opportunity to testify. I hope that you will consider us as a resource in the future.

[The prepared statement of Mr. Kelly can be found on page 139 of the appendix.]

Chairwoman BIGGERT. Thank you so much.

Ms. Bowdler, am I pronouncing that correctly?

Ms. BOWDLER. Yes.

Chairwoman BIGGERT. You are recognized for 5 minutes.

STATEMENT OF JANIS BOWDLER, DIRECTOR, WEALTH-BUILDING POLICY PROJECT, NATIONAL COUNCIL OF LA RAZA

Ms. BOWDLER. Thank you. Good afternoon. I would like to thank you, Chairwoman Biggert, and Ranking Member Gutierrez for inviting me here today. In my capacity as the director of the Wealth-Building Policy Project at the National Council of La Raza (NCLR), I oversee our research and advocacy on housing and financial services issues facing Hispanic families.

NCLR has worked tirelessly for decades to make homeownership possible for a greater number of Latinos. The NCLR homeownership network provides thousands of first-time home buyers objective advice and guidance each year. This work gives us a unique insight into the opportunities and challenges facing Latinos in the housing market. In fact, NCLR documented a number of systemic problems impacting Hispanic consumers prior to the market crash. The evidence and feedback from Latino service agencies led us to support the protections included in Dodd-Frank. While we wait for final regulations, NCLR has high hopes that the new rules will protect consumers while maintaining market access.

In my time today, I will briefly review those challenges, and then turn to three critical areas of mortgage origination reform currently under consideration. In testimony before the Financial Services Committee 2 years ago, NCLR President and CEO Janet Murguia shared four basic problems facing Latino housing consumers.

Briefly, they were that shopping for credit is nearly impossible. Few tools exist, so even the most diligent shoppers have a hard time making apples-to-apples comparisons. Borrowers are steered towards expensive products, even when they have good credit. Creditors trap borrowers in cycles of debt, and fraud and scams are rampant. The FTC has found that Latinos are more than twice as likely to become targets of fraud as Whites. This blatant pattern of overpayment, abuse, and discrimination disrupts the financial stability of low-income and minority households. In such an environment, deceptive actors have had their way at the expense of responsible lenders, homeowners, and taxpayers.

The protections established in Dodd-Frank responded directly to this situation. Well-implemented regulations should advance a mortgage market that treats consumers and honest dealers fairly and maintains a responsible flow of credit to qualified borrowers.

In response to questions raised during this hearing, we offer our perspective on three aspects of origination. The first is the revised TILA GFE disclosure being drafted by CFPB. As I mentioned, our mortgage shopping tools are inadequate. The GFE was supposed to play this role but comes too late in the process to be effective. NCLR applauds CFPB for their progress so far in developing and evaluating a new tool. The online feedback tool is transparent and allows for a broad audience to provide input. CFPB has also co-developed a Spanish language version of the disclosure. Word-for-word translations are often problematic and fail to communicate the same meaning, tone, and purpose as the English original. We urge CFPB to use their online tools to solicit comments on the Spanish version of the disclosure.

Also under debate is the Federal Reserve's rule on originator compensation. Steering was one of the most egregious deceptive lending tactics aimed at Hispanic borrowers. Simply put, originators were paid more for pushing creditworthy borrowers into loans with high upfront fees, interest-only payments, negative amortization, and exploding interest rates. Mortgage brokers play an essential role in helping Latino families purchase their home, especially when Spanish is their preferred language, but unfortunately this trust was violated by unscrupulous actors, causing irreparable harm to families and honest brokers.

Therefore, we strongly support the commonsense rule proposed by the Federal Reserve and further cemented by Dodd-Frank. This rule rightly prohibits compensation based on the terms of the loan while still allowing originators to be paid for their work.

Finally, NCLR urges this committee to consider the role of housing counselors in mortgage origination. Research has shown that borrowers who receive counseling before they buy are less likely to default. During the bubble years, housing counselors often delivered the tough "eat-your-veggies" message to consumers, often in direct competition with originators and REALTORS®. Rather than work with counselors, many industry players saw them as a roadblock to a fast and lucrative closing.

The elimination of funding for the housing counseling program is a huge loss for home buyers and communities of color in particular. We urge Congress to fully fund the program at $88 million in the 2012 budget.

I want to take a moment to especially thank the members of this committee, in particular Mrs. Biggert, Mr. Gutierrez, and Ms. Waters for your support and leadership. Members of this committee have been big champions of counseling. We appreciate that.

In sum, NCLR supports the mandates of Dodd-Frank that further responsible and accessible markets, reward honest lenders, and aid qualified home buyers and homeowners. I would like to make three modest recommendations: make the Spanish TILA form available for public comment; fully fund the housing counseling program; and swiftly implement the Federal Reserve's rule on steering.

Thank you, I would be happy to answer any questions.

[The prepared statement of Ms. Bowdler can be found on page 73 of the appendix.]

Chairwoman BIGGERT. Thank you.

Mr. Rheingold, you are recognized for 5 minutes.

STATEMENT OF IRA RHEINGOLD, EXECUTIVE DIRECTOR, NATIONAL ASSOCIATION OF CONSUMER ADVOCATES

Mr. RHEINGOLD. Thank you.

Chairwoman Biggert, Ranking Member Gutierrez, and members of the subcommittee, thank you for inviting me to testify today.

My name is Ira Rheingold, and I offer this testimony on behalf of the National Association of Consumer Advocates (NACA) and the low-income clients of the National Consumer Law Center.

I have been a public interest attorney for my entire career and worked in some of our Nation's poorest urban and rural communities. From the mid-1990s through 2001, I lived and worked in Chicago, where I ran the Legal Assistance Foundation's Home Ownership Preservation Project. During those years, I worked against the unfair and deceptive practices most of the actors in the mortgage industry were involved in.

Today, I am the executive director of the National Association of Consumer Advocates, an organization of attorneys who represent those very same consumers and communities all across this country. At NACA, I also manage the Institute for Foreclosure Legal Assistance, a project that provides funding and training to Legal Aid programs that assist consumers trying to save their homes.

Before I address recent changes to rules affecting mortgage origination, I think it is essential to put the recent reforms into the context of what the mortgage process looked like until its bubble burst and shattered our Nation's economy.

The mortgage market of the past few decades in no way resembles what most of us thought we understood about buying a home or getting a loan. I have talked to thousands of consumers who believed that the mortgage entity that originated their loan would only profit when they timely made their mortgage payment. While this may have been the case when our parents or even our grandparents bought their homes, this was not true for most of the past 2 decades.

Instead, because of the growth of securitization as a tool to fund both prime and subprime mortgages, with all its confusing layers, multiple actors and other perverse incentives, the nature of the consumer mortgage originator relationship, unbeknownst to the consumer, fundamentally changed.

No longer was the borrower's best interest or even their ability to repay the loan part of the mortgage transaction calculation. Instead, the real transaction was between the mortgage originator and the investment bank, not the borrower.

Under these circumstances, what American consumers needed was vigorous enforcement of existing consumer protections as well as a new set of consumer protections to correspond with the very different mortgage world that had now been created.

Unfortunately, what the Federal Government gave us was the exact opposite, not only diminishing its regulation and enforcement of this markets, but providing interference and protection under the guise of preemption for mortgage market players when States, recognizing the fundamental flaws in the system, attempted to protect their own citizens.

Despite the dire warnings of consumer advocates about the consequences of the clearly broken U.S. mortgage marketplace, it took a full-scale credit and mortgage meltdown before Congress finally and belatedly took action by passing the historic Dodd-Frank Act.

While discussing the merits of the important mortgage origination reforms created by this law, to me the question before our panel today seems to be extremely premature. Simply, we really won't know how successful the law will be in creating a fair and honest mortgage marketplace until we have a fully functioning housing market. Unfortunately, that won't happen until we effectively resolve the foreclosure crisis that continues to serve as an anchor on our housing market and on our overall economy.

Nonetheless, from a consumer's perspective, Dodd-Frank was an incredibly important piece of legislation. It not only created the independent and absolutely essential CFPB, but it also addressed most of the significant problems faced by everyday Americans trying to get a mortgage loan. So let's take a look at those provisions and how they should impact the mortgage market.

The banning of Yield Spread Premiums: The banning of YSPs may be the most important change in the mortgage origination landscape. Simply put, no longer will mortgage brokers be allowed to benefit by steering consumers into loans with high rates or other terms lucrative for the broker but harmful to consumers.

The banning of forced arbitration clauses: Restoring a consumer's right to hold mortgage banks accountable in court is essential to building a mortgage market that consumers can trust.

Limitation on prepayment penalties: Another one of the most abusive practices witnessed in the very recent mortgage market past, prohibiting prepayment penalties for non-safe-harbor mortgages should eliminate the problem of homeowners being trapped in expensive mortgage loans.

Requiring creditors to evaluate a consumer's ability to repay: Consumers were typically amazed and pretty appalled when I explained that there was no effective Federal law that prohibited mortgage originators from making loans that borrowers could not afford. Now that this has been remedied, I would hope that the mortgage industry would once again engage in fair and responsible underwriting of loans.

The expansion of HOEPA: By expanding the range of loans subject to HOEPA, it will not only provide consumers with much more robust protection from high-cost loans, it will hopefully provide a sufficient disincentive so that originators don't continue to make these disruptive loans.

Beginning to reform the appraisal process; creating safe harbor mortgages; and finally, a single integrated disclosure: Dodd-Frank required the CFPB to create a single integrated disclosure for mortgage transactions that combine the RESPA settlement statement and the mandatory TILA disclosures for mortgages.

For more than a decade, Federal regulators have struggled to create a fair and simple disclosure that gives consumers the essential information they need to both shop for a mortgage and openly choose wisely for themselves. Each time HUD or the Fed attempted to develop a form that offered some promise for consumers, objections arose from various single interest entities who feared that real honest and consumer-friendly disclosures might hurt their bottom line.

Today, almost 1 year since the passage of the groundbreaking Dodd-Frank legislation—

Chairwoman BIGGERT. If you can conclude, please.

Mr. RHEINGOLD. I am concluding. While the struggle continues—today, almost 1 year since the passage of Dodd-Frank, millions of former and current homeowners continue to battle to right themselves. While the struggle will continue until we finally and forcefully address the foreclosure crisis that continues to depress our housing market, we have great faith that the mortgage mandates of Dodd-Frank, if implemented properly, will go a long way in creating a fair and honest, consumer-friendly marketplace.

[The prepared statement of Mr. Rheingold can be found on page 198 of the appendix.]

Chairwoman BIGGERT. Thank you. Your time has expired.

I actually have a question for Ms. Bowdler and Mr. Rheingold, and that is, are you familiar with the RESPA Home Warranty Clarification Act that was talked about earlier, H.R. 2446, and could you comment on the bill?

Mr. RHEINGOLD. I can't say that I am incredibly familiar with it. I know enough about the home warranty issue and the RESPA process. I think my initial reaction to the whole notion is that we have always been concerned about what REALTORS® can sell to homeowners.

Consumers are a captive audience at that very moment, and the reason why RESPA was created was because of the concern that consumers who had this trust relationship could be sold most things by that REALTOR®. So, I think we have a real concern about any exception that allows a real estate agent to sell, even a home warranty, to consumers. If the home warranty is a good product and a useful product, then I think consumers will have the opportunity to buy it. I think there is a real danger there because of the nature of the trust relationship to have a real estate agent selling it.

Chairwoman BIGGERT. Thank you.

Hopefully, you will work with us on this bill.

Ms. Bowdler, would you like to comment on it?

Ms. BOWDLER. Only to say that the bill was just brought to our attention. We have not had a chance to fully review it. But we will take a closer look at it and definitely connect with your office.

Chairwoman BIGGERT. Thank you. I appreciate that.

Mr. Brown and maybe anyone else who is aware of this, are you aware of any study that HUD conducted on the home warranties or of complaints about the product or method of sales? Any complaints that have been filed with HUD?

Mr. BROWN. I am not aware of any study that they conducted, Madam Chairwoman, but it is a little ironic that the term used to describe the relationship between a REALTOR® and a home warranty is a mere referral.

Last week, I had meetings with the dominant provider of services for HVAC contractors, heaters, plumbers, etc., with 15 of our top agents, because we are trying to smooth out the problems that occur during the sale and processing and problems that they have after the sale. So the active engagement that agents perform in those services is undeniable, marketing from the time it starts until after closing, solving those problems.

Chairwoman BIGGERT. And do HUD's rules and guidance have any impact on jobs?

Mr. BROWN. I think it could. The warranty companies don't have sales forces. The modest amount of money that is paid to a real estate company for the presentation, marketing, explanation, and servicing during those problems, and as I just mentioned, after the sale problems that result with people who have problems with their systems breaking down—they go to their REALTOR®, or many times before they call them, they call the warranty company.

If they are not compensated, if they are not allowed to—we have agents today who say, why do I go through this process? The suggestion from HUD was to write down the serial numbers of systems as a compensable service, which does absolutely no good to the warranty company or anyone. So I think that consumers could actually be harmed if they take the REALTOR® out of that equation.

Chairwoman BIGGERT. Couldn't HUD's rule limit consumer choice and awareness and protections?

Mr. BROWN. They can. It is a very competitive industry. As I said before, the REALTOR® is the one who typically is involved in giving the consumer options at that time, and without their active involvement and active engagement in that process, I could see a limiting of the choices.

Chairwoman BIGGERT. Thank you.

Ms. Stephens, appraisals fraud and inflated appraisals, I guess, were two of the contributing factors to the financial crisis. You alluded to that fact, the fact that Congress may need to act to enhance appraisal oversight. Can you offer some suggestions?

Ms. STEPHENS. Yes. At all costs, I think that one of the most important things that needs to come forward from what we have seen with the fraud and the inflated appraisals is the push to professionalism and the push to people who are trained to do the work that a professional appraiser does, who has an education, who has taken the time to put themselves in a position to understand their market, to understand the nuances of a neighborhood and the areas in which they are working. Yes, ma'am.

Chairwoman BIGGERT. Thank you.

And one more question. The Dodd-Frank Act required Federal regulators to issue risk retention rules which require mortgage originators to retain 5 percent of the risk of a mortgage that is not in QRM and securitized and sold on the secondary market. On March 29, 2011, Federal regulators issued a proposed rule and solicited comments, but the deadline was extended until August 1st. Like the Federal Reserve's ability to repay proposed rules, one component of the risk retention rules requires that points and fees for a QRM not exceed 3 percent of the loan retention.

It seems like what has happened here is that these fees do not count toward this cap for third party settlement, but settlement fees of an affiliated business do. So does this mean that QRM standards and risk retention rules may result in increased compliance and legal costs for mortgage industry participants, but there are competing businesses that would be treated differently? Is this a level playing field?

Mr. WILSON. I think you summarized that correctly, and it does not—it makes it an unlevel playing field. So anybody who has affiliated businesses is at a disadvantage.

Chairwoman BIGGERT. And how could we fix that? Would it be legislation?

Mr. WILSON. I believe so. But I think endorsing the title exemption is the best way to do it, exempt title from those fees and services.

Ms. ANASTASI. Madam Chairwoman, we would also like to just reemphasize that if we are looking for a gold standard mortgage, we want to make sure there is a title insurance search and product associated with that to reduce the risk even further.

Chairwoman BIGGERT. That just amazes me, as a former real estate attorney, not having an owner's policy, It amazes me.

Ms. ANASTASI. It amazes us, too.

Chairwoman BIGGERT. Thank you.

Mr. Gutierrez, you are recognized for 5 minutes.

Mr. GUTIERREZ. Thank you so much.

I have a question for Mr. Brown, and let me just preface, and that is over the last couple of decades, every home I have either bought or sold has been with a member of the association that you represent. So I have had a wonderful relationship with them and look forward to my buying and selling, so you shouldn't take this as an indication about how I feel, because in my personal life, obviously, it should be reflected.

We have a new consumer protection agency that we are giving birth to pretty soon. So tell me, REALTORS®, your thoughts on that and the relationship going forward, things they should do, because I am sure you also represent the best interests of consumers, the very people that you serve every day.

Mr. BROWN. Absolutely. I think that they serve a proper role to ensure that the consumer is not taken advantage of. I am not certain that I am the person to ask for the entire scope of all of their services.

Mr. GUTIERREZ. Is there something you think they might consider doing that would help consumers and make the industry prosper?

Mr. BROWN. I think that in the vein of making sure that there isn't fraud in the lending process, that there is transparency in the process, simplification of rules and regulations, to the extent that they can make those types of changes and those types of protections—

Mr. GUTIERREZ. A consumer protection agency that would help make the process more transparent and less fraudulent for consumers would be a good thing.

Mr. BROWN. And not burdensome to business at the same time.

Mr. GUTIERREZ. Okay. Let me ask the same question of Mr. Cunningham.

Mr. CUNNINGHAM. I think that the benefit of the Consumer Financial Protection Bureau, the potential benefit, is they now have control of all the consumer laws related to mortgage lending. They have a unique opportunity to consolidate disclosures, disclosures that are, quite frankly, very consuming, sometimes conflicting to the consumer. So I think the biggest—

Mr. GUTIERREZ. Helping to facilitate a better understanding of the consumer in terms of the actual product they are going to acquire through better understanding or clarification or simplification of the documents that you might need.

Mr. CUNNINGHAM. Exactly right. I think that today, consumers sign documents without understanding them because there are so many, and there is a way to simplify that process.

Mr. GUTIERREZ. I assure both of you as soon as the obstacles for the new director—I talked to her—I am sorry, maybe him, because they might have their way. But thank you for those answers, because I am with you on those levels, and I would like to talk with you at any time about other things.

I am going to go over to Mr. Ira Rheingold. Tell me, you just heard from the industry, the mortgage association and the REALTORS®, what do you think?

Mr. RHEINGOLD. What do I think about the CFPB?

Mr. GUTIERREZ. What they said.

Mr. RHEINGOLD. I think that is a positive statement. I think that we all can agree that the way disclosures work in the mortgage process is pretty much disastrous.

Mr. GUTIERREZ. The number one thing the new Consumer Protection Agency can do?

Mr. RHEINGOLD. Do I think that is the number one thing they should do?

Mr. GUTIERREZ. No, no. What is the number one thing you think they should do?

Mr. RHEINGOLD. I think that taking the definition of getting involved in what a Qualified Mortgage is, helping define what a safe mortgage is as the statute requires, I think is a really important thing to do. I think beginning to take a look at TILA and RESPA, the abuses that exist, getting ahold of those regulations and making sure that they take enforcement actions when those laws are violated, but then also begin to investigate and use their oversight capacity to take a look at that.

Mr. GUTIERREZ. So some more enforcement—

Mr. RHEINGOLD. Enforcement and regulation.

Mr. GUTIERREZ. Ms. Bowdler, please?

Ms. BOWDLER. I want to say that I think that we have to keep in mind that CFPB is really important for all of the fair and honest businesses that are out there, too. In 2006, we did a series of interviews with Hispanic mortgage brokers serving the Latino community, and these were on-the-ground interviews in six different cities. And many of them were appalled by the practices that were going on and the bad name that their industry was getting and actually welcomed something to clean up the industry. So I think if CFPB is doing their job right, they are also on the side of the fair and honest dealer here.

I think one of the most important things the agency can take on is really incorporating fair lending into their oversight of lenders and making sure that the procedures and protocols are in place at the institutions that they are regulating to check for that. But it hasn't been a prominent part of the exams.

Mr. GUTIERREZ. You see, I think there is a way, Madam Chairwoman, that we can work to both benefit an industry that is on the side of creating the mortgages, the banking side, right, and the REALTORS®, who show everybody the house and make everybody understand what is in the market and help consumers, and at the same time, help consumers. Because as I go out there, I have to tell you, I have REALTORS® who are doing other jobs. They are not REALTORS® anymore, a lot of the ones I know. And it isn't because they are slackers or they are bad REALTORS®, because I remember when they were really busy. I know a lot of people in the mortgage banking industry who aren't busy. And I know Chicago Title and Trust and all the other title companies, there are lots of—you can get anywhere on the schedule if you want to go insure a home.

It seems to me there has been an overall collapse of the system, that it has been bad both for consumers and for those people in the industry, and you can't get this economy going again until you get the housing industry straight. Let's fix it so that you can all be prosperous and make lots of money, and people can get wonderful homes and make wonderful investments and have wonderful places to raise their children.

Thank you for your answers.

Chairwoman BIGGERT. I think that is what we are all looking for.

Mr. GUTIERREZ. I look forward to working with the gentlewoman.

Chairwoman BIGGERT. Mr. Hurt is recognized.

Mr. HURT. Thank you, Madam Chairwoman.

I want to thank each of you for being here this afternoon, and I guess I wanted to follow up with Mr. Savitt and his remarks relating to Ms. Braunstein and what she testified to in the earlier panel.

It sounds to me that perhaps you all do not have the clear guidance that you sought from the Federal Reserve as it relates to the loan originators compensation rule that was adopted in April. I was wondering if you could talk a little bit more about the effects of that, what effect it has had on your business, and what do you need from the Federal Reserve Board or from the CFPB going forward to help solve your issues?

I was hoping, I would like to hear from Ms. Anastasi and Mr. Anderson as well, if you could also follow up.

Mr. SAVITT. The effects have been devastating. It actually has turned out worse than we even thought it was. The Federal Reserve Board themselves indicated in their rule that there would be a significant economic—I am trying to think of their exact words—impact, a significant economic impact on small entities, but they never elaborated on that.

The Federal Reserve Board has given absolutely no guidance whatsoever. I have had conversations, both in email and on the telephone, with their Community Affairs Office asking them for clarification. I actually had one of them write back and say, "We don't answer anything in writing."

So, we have a tremendous problem with this. We have to proceed very cautiously. We are not sure if we are doing things right or not, which could put us in trouble with regulators.

Speaking of regulators, the regulators have told me in numerous States that they are also confused by this, that the Federal Reserve Board has provided no guidance whatsoever to them, and in many States, they are not even enforcing this; they are not going to regulate this, because they also don't want to make any mistakes. This has cost, as I said before, a tremendous amount of job loss. And it continues, and if we don't get some type of guidance, there won't be mortgage brokers very much longer.

Mr. ANDERSON. I actually agree with what Mr. Savitt just said. We are experiencing problems, severe problems. I had a loan officer quit yesterday. The guidance portion, we have asked the National Association of Mortgage Brokers. We have requested written guidance and we can't get written guidance. It is very, very complicated. We can't charge a processing fee. We can't charge the normal fees that we have normally charged. And when I said in my oral testimony that I am literally getting emails every day, the one I got yesterday is from a lady in Texas who has been in business for 10 years. She said she never participated in subprime loans. She shut her doors yesterday and said she couldn't take it anymore.

Madam Chairwoman, I would also like to add to the record a letter from the Honorable Barney Frank to the Federal Reserve.

Chairwoman BIGGERT. Without objection, it is so ordered.

Ms. ANASTASI. Thank you.

One of the things that we continually look for and that we all continually talk about is transparency. That is one of the reasons why we are suggesting that we go back to itemization of fees, so that the consumer understands completely what they are charging rather than the current way of rolling up the fees into certain categories.

We believe, along with everybody on this panel and everybody sitting in front of me, that clarity begets compliance, and without having answers, particularly answers in writing, to help protect us in our businesses, without having those answers, we are forced to make up and create the answers, and they may not necessarily be the correct answers.

So, we are simply asking for answers to questions, and I don't think that is too much to ask. Thank you.

Mr. HURT. Thank you, Madam Chairwoman. I yield back.

Chairwoman BIGGERT. Thank you.

The gentlelady from California, Ms. Waters, is recognized for 5 minutes.

Ms. WATERS. Thank you very much, Madam Chairwoman. I thank you for holding this hearing. You have an awful lot of people here representing various aspects of the mortgage industry.

I would first like to say that we all must accept some responsibility for the subprime meltdown and the economic crisis that resulted as a result of the meltdown. I accept responsibility as a Member of Congress sitting on a committee where we have oversight responsibilities. I think the regulators are going to have to accept some responsibility, and many of you in the industry have to accept some responsibility.

One of the most devastating aspects of the meltdown had to do with these exotic products that we have learned about. I am just wondering, to the brokers and the bankers, when you saw these products out there, what did you think? Did you think, something is wrong with this, but if the regulators say it is okay, I am going to use these products? Or did you think, maybe I ought to call somebody and tell somebody that I think this is wrong? And what can you do now? Given that we have gone through everything that we have gone through and even now that we have had Dodd-Frank and we are trying to help the consumer, do you think there are ways, given that you are the experts, that you could help the consumers and the Members of Congress move a little quicker when these things are happening?

Let me start with, I guess, the brokers.

Mr. ANDERSON. Like I said in the oral testimony, I am going to use an example of—remember the Ford Pinto? It was a bad product. And what did you do? You got rid of the product. You didn't go after the salesman, the auto salesman who sold it. And when the subprime market came out, and I commend you for saying, we all need to take responsibility, and you are right. There is enough blame to go around.

But I can tell you, I remember just Fannie Mae and Freddie Mac loans, I remember sitting around after work and having a beer with colleagues and saying, can you believe that we are getting loans approved through Fannie Mae and Freddie Mac, 100 percent with a 65 percent debt-to-income ratio with a 550 credit score? We did have those conversations. Those of us in the industry knew that this day was going to come.

With that said, like that chart illustrates that was supposed to be displayed here, we know what caused the crisis. It was the loan product. If you take that product off the shelf, it is a simple fix. And if you look in our State of Louisiana, 13 percent of our business was subprime. I hope that answers it.

Ms. WATERS. All right, let me go to another question rather than continue down this line. The President admitted just a few days ago that if there is any failure that they have had, it is in dealing with this crisis and loan modifications and an inability to create a program that would really assist the homeowners in a credible way.

We know that they had the HAMP program, and it did not work. Now he is talking about the ability to keep people in their homes for at least one year if they qualify. But it doesn't cover Fannie and Freddie.

We need help in designing a program to deal with loan modifications that is credible. One of the things we experienced when we got into this loan modification business was the servicers were not always qualified. They had to get up to speed in training them. I personally called and talked to servicers, got waivers from homeowners to do so. They lost papers. That was the name of the game. "We lost your papers. Submit them again." They didn't take into consideration all of the streams of income, whether it was child support payments, etc., etc., etc., on and on and on.

One person, give me your take on what we can do to have a good, sound loan modification program that works? Anybody?

Mr. SAVITT. You can start with a timely response, Ms. Waters. A lot of the problems with the modifications that we have seen, a borrower or a homeowner will submit their paperwork to the lender and it takes forever to get an answer, and they tell them that you have to be at least 2 or 3 months behind. So, they get 2 or 3 months behind intentionally as a recommendation from their lender, and then later on down the road, when they finally do get a response from the lender, it is a no and now you have somebody who is at the point of going into foreclosure. So, I think some of those things need to be corrected first.

Mr. RHEINGOLD. I think there are so many things. I think Congress had the opportunity with traditional modification, and unfortunately that failed. That would have made a gigantic difference in making loan modifications happen. I think the problem is we have never mandated that these things happen. It has always been sort of this "please do it, we are giving you incentives to do it," but it has never been mandated. I think that has been a serious failure.

I think finally there has to be principal reduction in foreclosures. There has to be. Because we are not going to get the housing market stabilized. The housing market is flooded with homes that are being foreclosed, with people underwater, and until we bring housing prices down to where they really need to be by dealing with all those foreclosed properties, we are not going to solve this problem.

Mr. CUNNINGHAM. I think also national standards for servicing are important. I think that MBA has been proactive in taking a position, having a study as it relates to that, and we would be glad to share that study with you after this hearing.

Ms. WATERS. Thank you, Madam Chairwoman. You have been very generous.

I would certainly hope if you submit to the Chair that study, she would make it available to all of us.

Mr. WILSON. Could I add, I work with the large lenders on both modifications and short sales, and as you want rules around making the new loans, debt-to-income ratios and fully doc loans, you almost can't have those rules on modifications. We created so many rules in HAMP, that nobody qualified, and there was no long-term solution for that borrower. So, the same rules you want as you are originating new loans can't apply, unfortunately, to the existing modification program.

I think there has to be regulated relief, both for the servicers, the banks, and the consumer, together. Because the banks are afraid to make one with a 42 percent debt-to-income ratio, even though that customer can in fact afford the payment if their interest rate is lowered. But they are afraid they will overstep their servicing requirements. There has to be regulated relief among those three for that to ever be a viable program.

Chairwoman BIGGERT. We are going to have to move on.

But, without objection, we will make the MBA's study part of the record.

Chairwoman BIGGERT. Mr. Stivers, you are recognized.

Mr. STIVERS. Thank you, Madam Chairwoman.

My first question is for Mr. Brown. You talked earlier about the home warranty issue. I know a lot of home buyers buy home warranties to limit their downside in case a major system fails. I was just curious if you think that the new HUD rules involving RESPA will result in less home buyers buying this protection from this downside?

Mr. BROWN. I can't say that I would think that their rules would necessarily decrease sales of warranties. I think that agents are going to do what is good for their clients in general. But what is happening is that they are just not being compensated for what they are doing. So they are not happy about it, I can tell you that. The things that they are being asked to do, to perform what is referred to as a compensable service, are absolutely absurd.

Mr. STIVERS. Let me ask it this way, Mr. Brown, do you believe that providing access to these home warranties is an important service to home buyers?

Mr. BROWN. It absolutely is. There is no question about it.

Mr. STIVERS. Therefore, it makes sense—have you heard of any home buyers complaining about their brokers getting compensated?

Mr. BROWN. No, and it has to be disclosed, and it should absolutely be disclosed beforehand. And it is, in the majority of the instances that I am aware of.

Mr. STIVERS. Thank you so much.

Mr. Cunningham, I wanted to ask you about the safe harbor provisions that were in your testimony. Can you help me understand why a safe harbor is important? I think it makes a lot of sense. Can you just help us understand the value of a Qualified Mortgage safe harbor for your members?

Mr. CUNNINGHAM. I would be glad to.

I think if rules are vague, a lender is going to be unsure, certainly has liability from a lawsuit and, therefore, is going to step way back from where the presumed line is and, therefore, reduce the availability of credit to consumers who might otherwise qualify.

If the standards are bright-line standards, then it is easy for a lender to comply, and it is at the same time easy for a consumer to show where they have not complied if a lawsuit is justified.

Mr. STIVERS. Thank you.

And the current QRM rules actually provide more harm to home buyers buying more affordable, less expensive homes, do they not, because of the percentages definitions in the qualifying mortgage?

Mr. CUNNINGHAM. You are talking about the Qualified Residential Mortgage.

Mr. STIVERS. Qualified Residential Mortgage.

Mr. CUNNINGHAM. Correct. If you just looked at my book of business in 2009, which was a pretty conservative book of business—referenced earlier that 97 percent of those were fixed rate. I applied those rules to our book of business; 58 percent of our purchase business and 74 percent of our refinance business would not have qualified.

Mr. STIVERS. Thank you. That is important to note.

The next question is for Ms. Anastasi. You talked earlier about how itemization and transparency is important so that home buyers can get the information that they need. Can you help us understand how home buyers shop for real estate settlement services?

Ms. ANASTASI. When a home buyer receives under the current rules the good faith estimate, on the estimate there is a section that describes the fees that are estimated to be charged for settlement services. They can simply pick up a phone, call other local providers, go on Web sites. Almost all of us have our own company Web sites. They can talk to their REALTOR® if it is a sale. They can talk to their mortgage lender if it is a refinance.

Mr. STIVERS. That is great. I just have one more question.

Can you help us understand some of the questions that home buyers are asking you at the closings that lead you to believe that more itemization and transparency are important?

Ms. ANASTASI. When you get to—on the HUD–1 settlement sheet, on page 2, line 1101, there is a roll up of all settlement services rolled up into one figure. When the consumer starts to shop, they don't know what is in that figure from the GSE estimate. But they ask us what is included, and we start going through the litany of what is in there. We are asked by the mortgage lenders—

Mr. STIVERS. They can't still tell, shop fee-by-fee. They can't tell, because it is not itemized, right?

Ms. ANASTASI. They cannot. We are not allowed to itemize on the HUD–1 settlement sheet. We are forced to do addendums to satisfy our lenders, to satisfy VA, and more importantly, to satisfy the consumers, so they know what it is from.

Mr. STIVERS. Thank you.

My time has expired. I yield back.

Chairwoman BIGGERT. Thank you.

Mr. Sherman, you are recognized for 5 minutes.

Mr. SHERMAN. Ms. Anastasi, I have additional questions for you. In your testimony, you said that disclosures need to be flexible to account for local practices. How can a single disclosure form be made flexible enough for every part of the country, and can you explain how buying a home in Illinois is different from buying a home in a much nicer place to live, namely California?

Chairwoman BIGGERT. Now, wait just a minute here.

Ms. ANASTASI. Good to see you, Mr. Sherman.

We need flexibility not only in the form but in what we are being forced to put on the form. Right now under the rule and what is expected in the new combined disclosure is that any fee that could possibly be charged to the buyer has to go on the GSE, even though in parts of California or in parts of Pennsylvania, that particular fee is always paid by the seller or it is contractually—the seller is contractually obligated. So, force-feeding fees into the GSE on the buyer's side, force feeding fees on to the HUD– 1 settlement sheet on the buyer side is just so confusing for the consumer.

And flexibility, give us a couple of extra lines. Let us itemize, but do not force the lenders to put a fee on the GSE that is not going to be paid for by the buyer.

Mr. SHERMAN. Are you objecting to just the fact there is a line for that fee and you would put a zero next to it, or—

Ms. ANASTASI. You are not allowed to put a zero next to it. That is the problem.

Mr. SHERMAN. So, there may be a line indicating that I, as the buyer of a home, may have to pay some sort of fee in a State where I am never going to have to pay the fee?

Ms. ANASTASI. That is exactly correct, or in the contract that has been negotiated to be paid for by the seller.

Mr. SHERMAN. And you can't put on that line "zero" or "seller pays." You have to leave me worrying that somebody is going to put a dollar figure in that and I am going to get hit with a charge of a type that I am not going to get hit with?

Ms. ANASTASI. You are exactly correct. I often talk about how we have to do a wink and a nod to the consumer saying, "I have to put this here, but don't worry, you won't get charged."

Mr. SHERMAN. Some of us have grown skeptical over the years, even when it is true.

Mr. Anderson, I heard the testimony of the Director of the Federal Reserve Division of Consumer Affairs, Ms. Braunstein, and I was pleased to note that she believes that brokers can now compensate their employees through commissions on consumer-paid transactions. I understand that this represents a change in their policy.

Does this change alleviate your concerns about loan officer compensation, or do we need to do more?

Mr. ANDERSON. When she said that, in the written testimony, I was surprised. We have not been notified of a change in the compensation. So that is the communication channel that we are not receiving.

There is more to it—

Mr. SHERMAN. It just means she told us before she told you.

Mr. ANDERSON. This was news to me. I have not heard that. So it would certainly be—

Mr. SHERMAN. Have you had enough time to look at that and can you comment on it, or does the fact that you were blindsided on it mean that in order to get your informed opinion, I will have to wait a few days?

Mr. ANDERSON. I would really like to review it. It is not that I don't trust them, but I would like to review it. But I will tell you, it is a start if we are allowed to pay our loan officers a commission on a consumer-paid transaction, if that is what she is referring to. But we would certainly like to review it.

Mr. SHERMAN. I yield back.

Chairwoman BIGGERT. Thank you.

And now the other gentleman from California, Mr. Miller, is recognized for 5 minutes.

Mr. SHERMAN. Whom I am sure agrees with the observation I made earlier.

Mr. MILLER OF CALIFORNIA. If the California State legislature doesn't screw the State up worse than it already is, I agree with you.

But right now, the inability of the market in this recession to strengthen itself is causing huge problems, and it is just a lack of consumer confidence we are facing. You are all seeing it in your areas.

People need to be confident their home prices are not going to continue to fall every week like they have, and they need to know that mortgages are going to be available today, tomorrow, and the year after.

But in Washington, we are doing some strange things, like conforming loan limits in high-cost areas. We are talking about eliminating them and dropping them right in the middle of a crisis when they have shown to do some good.

GSE reform, I don't think there is a doubt Freddie and Fannie have to go, but you have an alternative to them to provide liquidity for the marketplace. And the concept of just getting rid of them, if you don't have an alternative, you have no concern for the health of the marketplace, and that has to be dealt with specifically.

There are several issues that I am very interested in with respect to mortgage finance and homeownership. I am concerned with QRM. How they define this in the rule is going to be a huge problem. The SAFE Act, I am concerned about the overreach on equal application of the licensing requirements. The appraisals, I want to make sure the regulations are consistent across agencies. That has to take place. The merger of RESPA forms and truth in lending form, this is an important goal but must be undertaken very carefully to avoid consumer uncertainty, confusion and misinformation.

But the loan origination compensation, that application has to be considered nothing but a joke, at best. The Fed rule on loan origination compensation is more restrictive than was intended, even under Dodd-Frank. The compensation of employees, the rule creates a problem for mortgage brokers to compensate their employees in a way they have always done. It does not allow for commissions, but that is customary.

The lowering of compensation at closing of corrections, how can they restrict that? The lowering of compensation benefits the buyer, and in many cases, they are doing that just to make sure the loan does close. It is not a benefit to the broker at all. In fact, I am introducing a bill today to deal with that specifically. It has to be dealt with.

But on GSE reform, housing is critical to stabilize the economy, without a doubt. Private capital must be the dominant source. The government must have some continuing role. If you don't, you have no confidence in the system whatsoever.

Mr. Anderson, I enjoyed the testimony from all of you, but why shouldn't brokers be allowed to compensate their employees through a commission split versus an hourly wage as is being discussed?

Mr. ANDERSON. So we can be on a level playing field with the bank next door, Congressman. It has been that way for years. They work hard. The bank next door can do it, but we are prohibited as a mortgage broker.

Mr. MILLER OF CALIFORNIA. When you are talking about adjusting a loan, couldn't the current regulation result in the inability to close a loan at the last moment, by not allowing you to modify your fees?

Mr. ANDERSON. Right. We should be—it happens all the time, or used to happen all the time, that we would lower our compensation at the closing table.

Mr. MILLER OF CALIFORNIA. Let's give the example that you give an estimate of an appraisal, maybe $500. It comes back a day before closing at $750. In many cases, the mortgage broker will drop his commission $250 to allow the loan to go ahead and close. Has that been a problem?

Mr. ANDERSON. It is now.

Mr. MILLER OF CALIFORNIA. But has it ever in the past when you did that?

Mr. ANDERSON. No. We always did it.

Mr. MILLER OF CALIFORNIA. By allowing mortgage originators to reduce compensation at closing, let's say by a cap of 30 percent, do you think that would mitigate the potential for consumer abuse in the issue?

Mr. ANDERSON. I don't see how it would have any abuses. It would certainly help the consumer.

Mr. MILLER OF CALIFORNIA. Would you believe 30 percent is adequate?

Mr. ANDERSON. It certainly is a start. I would say, try it.

Mr. MILLER OF CALIFORNIA. Can you give me an example of when a mortgage origination would want to reduce compensation at closing besides that?

Mr. ANDERSON. We have a lot in our State because of insurance issues. We find out at the last minute that flood elevation is at a certain level and the insurance premium goes up by $300 or $400. We are all at the closing table, and we all pitch in to help that consumer. Because there are sellers and buyers, and you know how it goes. It has been a great exercise that we have done for years, and now the broker cannot do this any more.

Mr. MILLER OF CALIFORNIA. The issues I have just touched on, we could spend hours talking about them, but if we could take care of these issues, if we could eliminate Freddie and Fannie and have another facility that did the same purpose of providing private-sector dollars into the marketplace with certainty, do you believe it would have a major impact on the future of the housing market?

Mr. ANDERSON. Yes, I do, and I think this would be a good question for the bankers as well.

Mr. MILLER OF CALIFORNIA. Let's hear the bankers address it. I know how difficult it is for you. But you make many loans that you plan on selling off to the secondary market, and it allows you to have the liquidity to make more loans. And you service those loans, you make the loan origination fees. If we could resolve these issues, do you not believe the market would start to turn?

Mr. CUNNINGHAM. Define which issue you are trying to resolve.

Mr. MILLER OF CALIFORNIA. The issues I have talked about that we are dealing with in the marketplace overall. Like right now, you can't even in California, they won't accept a loan application for a conforming loan limit of 730, even though it doesn't expire for a while, because they can't process it in time.

Mr. CUNNINGHAM. We certainly support extending the loan limits to at least December 31, 2012. I think you can't reduce the loan limits now when the market is as fragile as it currently is.

Mr. MILLER OF CALIFORNIA. What percentage of your loans do you sell out to GSEs, would you guess?

Mr. CUNNINGHAM. Today, most of our loans are either FHA, VA—

Mr. MILLER OF CALIFORNIA. Ninety-two percent. Now, if they are not there, what do you do?

Mr. CUNNINGHAM. Probably 97 percent.

Mr. MILLER OF CALIFORNIA. What do you do if they are not there?

Mr. CUNNINGHAM. It would be a significant problem. There would be no liquidity in the marketplace.

Mr. MILLER OF CALIFORNIA. If we are going to protect taxpayers, let's do everything we can to make sure the value of their home does not plummet, because if you can't buy a home or sell a home, homes aren't worth anything. So when Congress says, we are trying to protect taxpayers, we need to look at the real issue, who are we protecting and how are we doing it.

You have been very generous, Madam Chairwoman. I yield back the balance of my time.

Chairwoman BIGGERT. Thank you, Mr. Miller.

I have just one further question, and that is for Mr. Kelly. I asked Ms. Braunstein this question earlier talking about the appraiser independence provision of the Dodd-Frank Act, Section 1472, which requires lenders to compensate appraisers at a rate that is customary and reasonable, and the Fed has issued a related rule. Do you think that this provision in the Dodd-Frank Act should be repealed, or do agree with it?

Mr. KELLY. We believe that the Fed has done a good job with following the intent of Congress. In fact, you heard from the Fed today that they structured a rule based on the reasonableness and the market conditions of applying all the factors that are exigent with any appraisal product. So, we think that while the language of the Dodd-Frank Act was not perfect, certainly the efforts of the

Fed to resolve the customary reasonable fee issue have been satisfactory.

Chairwoman BIGGERT. Thank you.

Ms. Stephens, do you agree with that?

Ms. STEPHENS. It is my understanding that one of the major provisions in the Dodd-Frank reasonable and customary fee is that it is exclusive of a fee to the AMC, that this is the fee that the appraiser would receive. And I don't think that is happening in a lot of instances. We are not hearing that from our members, and certainly we are not hearing that from other members of the appraisal profession.

Many of our folks are working at fees that are 40 to 60 percent what they were making before, and I think that is incumbent on this group and on your committee, please, to look into this and to see if we can't make some kind of provision that is fair and that gives our appraisers fair compensation for the work that they do and the expertise they possess.

Chairwoman BIGGERT. Thank you.

With that, I would like to thank all the witnesses and just say that early this fall, in September, which seems like it is coming very soon, this subcommittee is going to hold a hearing which will focus solely on housing counseling, which is certainly a critical step for new homeowners and those facing foreclosures and seniors who are seeking a reverse mortgage. So if any of today's witnesses would like to comment on HUD's program, appropriations or any other matters relating to housing counseling, please feel free to submit additional comments for today's hearing record. We would appreciate it.

With that, I would note that some members may have additional questions for this panel, which they may wish to submit in writing. Without objection, the hearing record will remain open for 30 days for members to submit their questions to these witnesses and to place their responses in the record.

With that, thank you again. This hearing is adjourned.

[Whereupon, at 5:05 p.m., the hearing was adjourned.]

A P P E N D I X

July 13, 2011

Opening Statement by Robert Hurt for 7-13-11 IH Subcommittee Hearing on "Mortgage Origination: The Impact of Recent Changes on Homeowners and Businesses"

I thank the gentlelady for yielding, and I am grateful for her leadership as this subcommittee conducts another hearing today to examine the ways in which federal regulations are affecting the housing market.

As we approach the one-year anniversary of the Dodd-Frank Act, the Financial Services Committee has conducted important oversight of this sweeping law and the many sectors of the economy that it affects. It is critical that we closely monitor the litany of rulemaking activities required by this law and ensure that we understand all of the potential consequences of its implementation.

In the context of today's hearing, we consider that not only are a number of new rules in development relating to mortgage origination, but also that many of those rules, along with existing regulatory mechanisms, will soon shift from various federal agencies to the Consumer Financial Protection Bureau. We should examine the scope of each individual rule on its merits, and we must also consider the effects of the entirety of the regulatory framework during this time of transition.

While no one disputes that we should take appropriate action to protect consumers, we must not allow poorly crafted regulations to harm the very stakeholders that they are intended to benefit - in this case, prospective homebuyers and current homeowners. It is more important for these regulations to be effective rather than excessively prescriptive. Effective regulation will draw private capital back into the housing market and facilitate a sustainable recovery in this vital economic sector.

Again, I'd like to thank Chairman Biggert for holding this important hearing today. I look forward to hearing from the witnesses. I yield back the balance of my time.

Mortgage Origination:

The Impact of Recent Changes on Homeowners and Businesses

House Financial Services Committee

Subcommittee on Insurance, Housing and Community Opportunity

Wednesday, July 13, 2011
2:00 P.M.

AMERICAN
LAND TITLE
ASSOCIATION

TM

My name is Anne Anastasi and I am the President of Genesis Abstract, LLC in Hatboro, Pennsylvania. I have been in the land title insurance industry for 33 years, and I hold Pennsylvania's Certified Land Title Professional designation, which is the highest designation available in the title industry.

Currently, I serve as the President of the American Land Title Association. ALTA, founded in 1907, is the national trade association and voice of the real estate settlement services, abstract and title insurance industry. ALTA's over 3,800 member companies operate in every county in the country, where we search, review and insure land titles to protect consumers and mortgage lenders who invest in real estate. ALTA members serve as independent, third-party facilitators of real estate transactions. We do not represent the borrower, lender, seller or any other party in a transaction. ALTA members include title insurers, title agents, independent abstracters, title searchers, settlement agents and attorneys, ranging from small, one-county operations, to large, national title insurers.

On behalf of ALTA, I appreciate the opportunity to appear before you today to discuss mortgage origination issues. My testimony will focus on the very end of the mortgage origination process, the closing. At closing, ALTA members serve as the independent, third-party facilitators of the real estate transaction. It is in this role that ALTA members are called upon for two major purposes. First, we ensure that the transaction is closed quickly, honestly and in accordance with all the parties' instructions. Second, we serve as the last resource for consumers when they have questions about their transaction.

As we seek to improve the mortgage origination process, we need to fundamentally rethink a key part of the architecture of the current process: federal mortgage disclosure laws. These laws are primarily designed to help consumers shop for mortgage and settlement services by providing them with timely information about their transaction. While this goal is laudable, from our vast experience at the closing table, the execution reveals some shortcomings that actually cause confusion and may be counterproductive for consumers.

Overview of Closing Process

When an individual participates in a closing to buy, or sell a home or refinance their mortgage, the main reason that such a complex real estate transfer can be quickly accomplished is because an independent, third party professional has already pulled together all of the documentation necessary to close the transaction. The closing process differs state by state and in some cases county by county, but the outcome is roughly the same in every jurisdiction.

Closing – or settlement as it is known in some parts of the country — is a term used to designate the point in time at which the contemplated transaction is concluded. For most residential purchase and sale transactions, closing generally designates the point at which title to the property is transferred from seller to buyer, a mortgage (or "deed of trust") is given by the buyer/borrower to the lender and the funds from the buyer and lender are transferred to the seller. The closing date is typically negotiated between the buyer and the seller along with other terms when they agree to a purchase contract.

Once a closing date is selected, the parties will select a closing or settlement agent. Consumers can shop around to select a settlement agent to perform the closing functions, or they can rely on a recommendation from their real estate agent or lender. While variances occur throughout the country, a closing agent is typically an attorney, or an employee of a title company, or escrow company. The closing agent acts as a clearinghouse collecting all the necessary documentation, including the deed, mortgage, title and homeowners insurance policies, payoffs (if there are liens on the property that must be released) and pest inspection reports. This person also handles the exchange of monies, including any earnest money deposit, mortgage funds and personal funds of the parties. Lastly, the closing agent prepares the Settlement Statement. The HUD-1, as it is referred to, documents all costs for both the buyer and seller associated with the closing and is required to be issued on all federally-related mortgage transactions.

At closing, the property is transferred from the seller to the buyer. In most parts of the country, consumers will sign a number of documents whose content will be described by their closing agent. Finally, the settlement agent will forward payment to any previous lender, other lien holders, tax collectors, municipalities and pay all of the other parties who performed services in connection with their closing, pay out any net funds to the seller, and order a final search of the title to their new home before finally recording all of the documents needed to complete their purchase.

This process can be daunting, but thanks to the efforts of closing agents and the American property rights recording system, transactions are most often closed in 30-45 days after signing the purchase agreement. It is worth highlighting that the United States enjoys one of the fastest transaction times in the world due to this public private partnership.

The Federal Disclosure Regime

In 1974, Congress passed the Real Estate Settlement Procedures Act. In Section 1 of RESPA, Congress declared that, "significant reforms in the real estate settlement process are needed to insure that consumers throughout the Nation are provided with *greater and more timely information on the nature and costs of the settlement process* and are protected from unnecessarily high settlement charges caused by certain abusive practices that have developed in some areas of the country." (emphasis added) A similar sentiment was expressed when Congress passed the Truth in Lending Act in 1968[1].

For mortgage transactions, these Acts mandate a two part regime of providing consumers with an early disclosure and a late disclosure of loan and settlement costs. This regulatory requirement has fundamentally shaped how mortgages are originated today.

Within three days of applying for a mortgage, consumers receives two disclosures: 1) an estimate of their loan terms and 2) an estimate of the closing costs (called the Good Faith Estimate or "GFE"). These documents are designed to help consumers shop for their mortgage by giving them estimates of their mortgage and closing costs that they can compare between competing lenders. On the current Good Faith Estimate, HUD includes a "shopping chart" to help assist consumers in comparing mortgage offers. However, despite the focus on consumer shopping, these early disclosures often are insufficient to help consumers shop because the form masks certain charges by reflecting only a combined cost number for several services, or "roll-up," which ultimately makes it more difficult for consumers to shop effectively for individual services.

After picking a loan product, consumers receive final disclosures at the closing table which outline the actual loan terms and the final closing costs called the Uniform Settlement Statement or HUD-1. Recent reforms have turned the HUD-1 from a simple disbursement sheet outlining all the fees paid at closing into a comparison document to help consumers compare their GFE and HUD-1 to assess the accuracy of the estimate and ask informed questions about whether costs changed and, if so, why they changed.

While these are the main disclosures given to consumers, other federal, state and local laws require that consumers be provided a myriad of additional disclosures at closing.

[1] "The Congress finds that economic stabilization would be enhanced and the competition among the various financial institutions and other firms engaged in the extension of consumer credit would be strengthened by the informed use of credit. The informed use of credit results from an awareness of the cost thereof by consumers. It is the purpose of this subchapter to assure a meaningful disclosure of credit terms so that the consumer will be able to compare more readily the various credit terms available to him." 15 USC 1601(a).

Policy Recommendations

In conducting closings, ALTA members find that consumers benefit most from disclosures that provide them with tools to more fully understand their individual transaction. ALTA would like to make the following recommendations to improve federal mortgage disclosures to ensure consumers receive the information needed for them to shop for their mortgage and settlement services.

Disclosures should be transparent so that consumers can get a complete view of their transaction

Improving transparency by itemizing costs will help consumers understand their entire transaction. One significant change to the RESPA disclosures adopted in November 2008 and implemented in January 2010 was the introduction of "roll-up" lines and aggregate line item totals on the HUD-1 Settlement Statement. This concept was designed to help consumers shop for settlement services by making it simpler to aggregate classes of charges. While the stated goal was improving consumer understanding of charges, roll-ups have not been an effective tool for achieving this goal. Rather, our experience has found that transparency, simplicity and itemization of charges is a more effective solution for consumers.

In the current forms, roll-ups lump fees into aggregate standard categories. Consumers are then encouraged to shop based on these aggregates. Alongside or underneath the aggregate, some (but not all) fees are itemized. Thus, consumers are given a disclosure that includes an aggregate fee that may not reconcile with an addition of the itemized fees listed underneath or alongside.

ALTA members routinely see the confusion this causes for consumers who are unable to reconcile the numbers on the page. A better solution would be to return the itemization and transparency from the previous GFE and HUD-1. Just like when you go out to dinner, your check doesn't just give you a total price. Rather, each item is listed giving you a breakdown of what you pay for. These forms would allow consumers to see where their money is going and to better inquire regarding fees they find questionable.

Itemization would also help consumers shop. Greater transparency of the source of costs helps consumers see what costs are included in the cash needed to close. This level of transparency offers a better opportunity for consumers to shop for these additional services by providing them detailed information to use when going to other providers to obtain competing bids. This level of detail and transparency promotes competition among providers, thus avoiding excessive fees and promoting a realistic picture of the transaction. Finally, this level of detail promotes consumer education by allowing consumers to look inside their transaction and have a better understanding of the fees they incur for various services.

Disclosures should include accurate estimates so consumers can make informed decisions about their transaction

Consumers' ability to shop for their mortgage and settlement services is improved when the estimates provided are accurate. However, we have found that attempts to tie initial estimates to final costs through the use of tolerances have not resulted in consumers receiving accurate estimates.

Currently, two categories of fee estimates are subject to restrictions on their increase from the numbers originally shown in the GFE. The first, which includes a lender's own charges and government transfer taxes, may not increase by any amount at closing. This category is often referred to as "zero tolerance". The second category includes services required by the lender where the provider is not selected by borrower lender. These costs, in the aggregate, may not increase by any more than 10% at closing. Should costs increase in excess of the tolerance allowance, a payment must be made by the lender of the amount in excess of the allowed tolerance.

While designed to provide more accurate disclosures, tolerances have had the opposite effect. To avoid a tolerance violation, some providers overestimate fees within their control that are subject to tolerance. These overestimations allow providers to ensure that even if some fees outside of their control increase, there will be a sufficient buffer to prevent a tolerance violation. Even if a tolerance violation occurs, many consumers express surprise at the prospect of the refund, and show no understanding of the tolerance concept.

Another way that some providers avoid tolerances is by issuing multiple initial disclosures during the transaction. Since only the most recent GFE is disclosed to the settlement agent for the computation of tolerances, these "magic GFEs" (as they are called in the industry) typically appear numerous times throughout the process to update the estimates to avoid a violation. The volume and frequency of the issuance of these "magic GFEs" (even though currently either prohibited or severely restricted by current RESPA regulations) have led some consumers to admit to ALTA members that they do not even open the new disclosures that they receive.

The effect of these practices is that tolerances are not necessarily resulting in more accurate estimates at the time of application or improved consumer comprehension. Thus, they fall short of their intended purpose.

Regulators should consider the impact new or altered disclosures will have on actual closings instead of isolated interviews with consumers

While disclosures represent only a small fraction of the documentation presented at closing, they are one of the few parts of the process that is growing. In my home state of Pennsylvania, a typical closing package includes 60-75 pages of documents. Each one of these documents must be reviewed with the consumer before they sign them at closing. This can be a time consuming process and usually ends with the consumer having a sore wrist and confused mind.

This whirlwind of documents may also have a negative impact on consumers. As a closer, I frequently deal with consumers who, in the face of the stack of documents they need to sign, simply give up and sign without taking the time to understand the contracts and obligations that they sign. Better efforts should be made to ensure that ever increasing government disclosures actually help consumers rather than hinder their understanding of their transaction.

To achieve this, qualitative testing of disclosures must take place in the context of the greater transaction to ensure that policymakers grasp the true impact that these forms have on consumers' understanding of their transactions. During the last round of RESPA Reform in 2002-2009, consumer testing took place in a vacuum where the testing of the GFE and HUD-1 done individually instead of as part of a greater transaction. While the new forms passed that testing, many ALTA members find that consumers are having a more difficult time, rather than a less difficult time understanding their costs.

At closing, typically four federally-required disclosures are provided to the consumer: the HUD-1, the Truth in Lending Disclosure, the Itemization of Amount Financed and the Lender's Right to Transfer Servicing Rights. These documents are all intended to inform consumers about the specific aspects of their transaction.

Since these disclosures have a common goal, Congress has repeatedly asked regulators to attempt to combine these disclosures into a single document. However, this task has proven daunting since many of the underlying federal statutes and regulations have differing terms, definitions and timing requirements. These divergent structures make integration challenging. Greater efforts need to be taken by regulators and Congress if necessary, to combine disclosures and reduce the amount of paperwork required at closing.

Nationally mandated disclosures should be flexible enough to allow for variation to reflect the consumer's individual transaction

As the saying goes, all real estate is local. Unfortunately for consumers, federal mortgage disclosures do not take this axiom into account. While real estate closings and practices vary greatly across the country, HUD in its 2010 RESPA rule created a regime that forces transactions into a one-size-fits-all disclosure.

This was not always the case. Originally, RESPA disclosures allowed for some variation for local custom. In states and localities where custom does not follow the norm, these national disclosures make it more difficult for consumers to shop for, and understand the settlement services that they receive.

Disclosures should be flexible enough to account for regional variations in closing practices

There are a number of fees listed on the GFE and HUD-1 that, in large swaths of the country, are paid for by the seller instead of the buyer in the transaction. Despite this, the latest RESPA reform included strict requirements that ALTA members and other settlement agents list these fees as being paid by the buyer (with appropriate credits given on other lines). At closing, the closing agent must explain this structure to confused consumers.

One example of this paradox is Owners Title Insurance. In many parts of the country, including Southern California, Owners Title Insurance is paid for by the seller by custom or negotiation. However, the closing agent must disclose the policy as a charge paid by the buyer on the HUD-1. This causes confusion for the consumer, and must be explained at closing to the consumer. Other examples include certain real estate taxes, home warranties and inspections.

Make disclosures fit the transaction, not the other way around

Mortgage disclosures need to be flexible enough to disclose all transaction costs. However, the current HUD-1 is too rigid and strictly controls where fees may be disclosed and the number of lines in each category. This leads to many fees being either left off the form or disclosed on an addendum, making it harder for consumers to see their entire transaction. Greater effort should be undertaken to ensure that all fees in a certain category are shown in concert on the disclosure.

Disclosures should encourage consumers to make informed decisions about closing services

At a minimum, federally-mandated mortgage disclosures should not prejudice consumers against protecting their financial investment. Certain services purchased as part of the real estate transaction protect consumers' financial interests. Federally-mandated disclosures should encourage consumers to investigate whether the service is in their best interest.

The choice of words used to refer to certain services can greatly influence consumers' likelihood of purchasing those services and acting in their best financial interests. Against Owners Title Insurance serves as good example. Recent proposals use the term "not required" on the GFE to disclose to consumers the closing costs that are not mandated by the lender, but are available to consumer, including Owners Title Insurance. However, by calling a service "not-required," these proposals contain a less than encouraging implication that the service is of less value to consumers. This message prejudices consumers against considering these services, even when these services are often in consumers' best interests and protection.

ALTA strongly encourages policymakers to avoid using the term "not required" in these disclosures, and instead use terms like "recommended" or "advisable". These terms encourage consumers to investigate services like owner's title and make an informed decision. This concept was recognized by HUD in the current Settlement Cost Booklet where the guide encourages consumers to investigate these services, including an Owners Title Insurance policy, indicating: "If you want to protect yourself from claims by others against your new home, you will need an owner's policy." If we have learned anything from the foreclosure crisis, it is that consumers should be encouraged to investigate products like Owners Title Insurance that help protect the consumers' interest.

Timely disclosures help consumers make informed decisions about their transaction

Finally, ALTA members have found that disclosures will only be effective if they are timely. Currently, consumers have a right to request their HUD-1 up to 24 hours in advance of closing. However, in practice, few if any consumers are able to obtain their disclosure that early in the process. Delays in transmitting the lender's closing instructions and other documents not only prevent the consumer from receiving the HUD-1 in advance of closing, but also force the consumer to wait at the closer's office (often times with the moving truck outside) while the closing agent waits to receive these documents and rushes to complete the HUD-1.

Consumers would be better protected if they received their closing documents in advance of their closing. This added transparency would allow consumers to read through their closing documents before having to sign them. It would also improve consumers' understanding of the documents, as they would be able to take the forms to a trusted advisor for explanation. Lastly, it would allow consumers to review the terms to ensure that they are paying the correct amount they were quoted.

Conclusion

ALTA appreciates the opportunity to discuss our firm belief that one of the best ways to improve the mortgage origination process is to improve federally mandated mortgage disclosures. We strongly believe that consumers are best protected when they are able to make informed decisions about their transaction based on transparent and accurate information. ALTA is eager to serve as a resource to the Subcommittee and other stakeholders, and I am happy to answer any questions. Thank you.

National Association of Mortgage Brokers

Prepared Testimony

of

Mike Anderson, CRMS

Vice-President &
Chairman of Government Affairs

National Association of Mortgage Brokers

on

Mortgage Origination:
The Impact of Recent Changes on Homeowners and Businesses

before the

Subcommittee on Insurance, Housing & Community Opportunity

Committee on Financial Services

United States House of Representatives

July 13, 2011

Mike Anderson is a Certified Residential Mortgage Specialist ("CRMS") and is the Vice-President and Chairman of Government Affairs for the National Association of Mortgage Brokers ("NAMB"). Mr. Anderson is a licensed mortgage broker in the State of Louisiana with over thirty (30) years of industry experience, and is the president of Essential Mortgage, a wholly-owned subsidiary of Latter & Blum Realtors, which is headquartered in New Orleans, Louisiana and is the oldest and largest real estate firm in the Gulf South.

I. The Modern Mortgage Broker Business

The typical mortgage broker business operating in today's marketplace is an origination channel, existing alongside other competing origination channels, through which consumers can obtain credit to purchase or refinance their home. Not unlike an insurance broker representing a large number of carriers from which their customer can choose a product, the modern mortgage broker typically offers loan products from between ten and fifty different banks and lenders across the country through what is referred to as the "wholesale channel."

The modern mortgage broker origination channel is mainly comprised of individuals who have been top performers in their field while working for other origination channels, such as banks or mortgage lenders. These individuals, aspiring to the dream of owning and operating their own business, establish themselves in cities large and small, urban and rural, and generally hire between three and fifty employees, making mortgage broker entities a truly valuable small business participant in their communities.

The modern mortgage broker business model is centered on customer service. Mortgage broker businesses generally seek and obtain approval from numerous creditors to submit mortgage files for underwriting and closing in order to provide consumers with greater access to a wider range of mortgage products and programs than are typically available through other distribution channels.

II. The Impact of Recent Changes on Mortgage Broker Businesses & Consumers

The recent regulatory changes in our industry have had a profoundly negative impact on mortgage brokers and on consumers. However, before we specifically address *how* these regulations have affected our businesses and our customers, it is important to explore *why* these changes that were aimed at creating a more consumer-friendly borrowing environment have had mainly the opposite effect.

The primary reason why recent regulatory changes have done more harm than good for both businesses and consumers is that these regulations, by design or through implementation, disproportionately target individuals, entities, and the disclosure of information rather than addressing specific issues related to faulty products or bad behavior.

For example, in the pharmaceutical industry when a faulty product is discovered to be causing harm to consumers using that product, the U.S. Food and Drug Administration ("FDA") typically steps in and requires the distribution and use of such product to be discontinued. In such circumstances, the FDA does not attempt to impose further restrictions on the pharmacies or pharmacists distributing the product or the physicians who prescribe it.

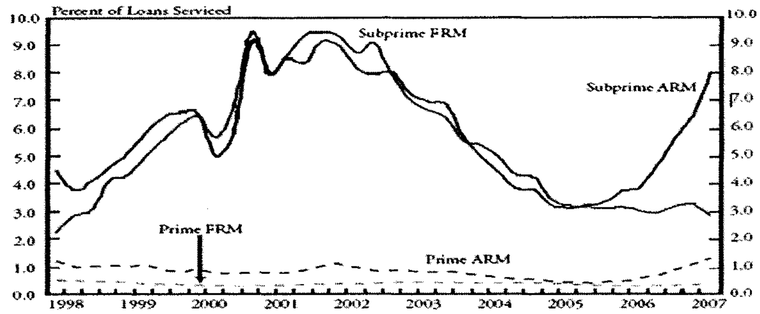
Unfortunately, exactly the opposite is happening in the mortgage industry. At the epicenter of our current mortgage and housing crisis are faulty loan products, such as the pay-option ARM, stated income, no-doc loans, and Alt-A and sub-prime mortgages. Much like a drug that was released onto the market, but later discovered to cause harmful and previously unforeseen side effects, these loan products were created and distributed in the mortgage marketplace before anyone really understood the potential for harm that these products brought to homeowners, entire communities and the economic stability of our mortgage and housing market.

However, unlike the FDA's typical response to the discovery of a harmful product falling within its purview of regulation, the Federal Reserve Board and Congress have gone far and beyond removing these harmful mortgage products from the shelves, which has led to a protracted economic recovery at best, and at worst has actually caused greater harm to the market than any faulty loan product has previously.

The chart below, created by the Federal Reserve Bank of Kansas City, helps illustrate the point that the largest underlying problem in our mortgage market has been the proliferation of faulty products.

Chart 4

FORECLOSURE RATES BY LOAN TYPE, 1998-2007



Source: *Mortgage Bankers Association*

Data for 2008 through 2010 are very similar as 1998 through 2007

However, despite evidence of the harm that these loan products have caused, the Federal Reserve Board and Congress have, to date, focused the vast majority of their attention, resources and regulatory authority on manipulating how providers of these products conduct their businesses rather than on how these products were created originally and why the harmful effects of these loan products were not realized until it was too late.

Recent regulations have been directed primarily at individuals, entities and disclosures within the mortgage industry and not at the products that are the root cause of so much of the economic damage consumers have already suffered. Because of these regulations, the livelihood of individuals and the survival many entities, large and small, within our industry is being severely threatened. Consumers too are already suffering, as competition continues to deteriorate and the mortgage marketplace becomes increasingly dominated by only a few of the industry's largest entities.

Consumer fees have increased substantially as lender and originator expenses per-loan are estimated to have risen by nearly $1,000.00 from the 4th Quarter of 2010 to the 1st Quarter of 2011. Consumers are also facing increased out-of-pocket costs for appraisals and higher loan fees in order to cover originators' costs in the event they are required to cure errors on the Good Faith Estimate ("GFE"), since the originator's compensation cannot be lowered. Additionally, many consumers are not receiving the time and attention they deserve from their loan originator, particularly if the consumer is seeking a smaller loan amount because such smaller loans have become increasingly unprofitable for the originators and their employers. In fact, in some areas, entities are instituting minimum loan amounts because it has become too cost-prohibitive for these entities to continue to originate smaller loans.

Additionally, there are far too many stories being relayed to us by our members and being shared in the media of highly qualified borrowers who are simply unable to obtain the mortgage financing they need to become homeowners or to transition into a larger or smaller property. This is in large part due to the glut of recent changes to underwriting, appraisal and credit score requirements, waiting periods and mortgage disclosures that have knocked the industry back on its heels and have severely stunted any progress we might otherwise be making toward economic recovery.

Across the board, entities in the mortgage origination business have seen their profits-per-loan drop by an estimated 66%, and individual loan originators have seen their compensation cut by 33% or more in some areas. According to a recent survey conducted by the Mortgage Bankers Association, the average per-loan profit for an entity in the 1st Quarter of 2011 was just $346, which was down from a $1,082 in the previous quarter, and down from $608 just one year earlier. The survey also found that 63% of the 329 responding firms posted pre-tax profits for the 1st Quarter 2011, compared to 84% in the quarter prior. While it's not unusual for profits to decline at the end of a refinancing boom, it is clear to many in the industry that this most recent downturn in profitability has been significantly more severe due to the increased compliance costs associated with the new regulatory requirements.

NAMB is gravely concerned that the recent changes promulgated by the Federal Reserve Board and Congress have done little to address the significant root causes of our mortgage and housing crisis, facilitate a recovery in the market, or create a more consumer-friendly mortgage lending environment.

III. Federal Reserve Board Rule on Loan Originator Compensation & Steering

In the few short months since the Federal Reserve Board's rule on loan originator compensation was implemented, mortgage broker businesses have suffered significant and irreparable harm as a result of these new requirements. However, what's worse is that these new requirements are having an even more profoundly negative effect on consumers.

Under the new rules, mortgage broker businesses can no longer accept compensation from both the lender and the borrower in connection with a loan transaction. Instead, mortgage brokers now are forced to choose, and in doing so limit their customers' ability to choose, whether the broker will be paid by the lender or the customer, but under no circumstance both. Additionally, the new rules prohibit a mortgage broker from ever adjusting its origination fee, once disclosed to the borrower, regardless of whether the price adjustment is down and for the benefit of the consumer.

An example of just one of the many ways that this rule is negatively impacting consumers was recently relayed to us by one of our members. This member was working with a customer that was prepared to close a loan on the purchase of a bank-owned property. One day before closing, the borrower's insurance company went out to physically inspect the property. As a result of this inspection, the insurance company raised the borrower's premium, making it impossible for the borrower to obtain mortgage insurance. Prior to implementation of the Board's new rules, the mortgage broker would have been able to reduce his/her fee for originating the loan and thereby reduce the borrower's interest rate and allow the loan to close as scheduled. However, under the new rules, this same borrower is forced to either delay closing and attempt to find a more affordable insurance provider, put substantially more money down upfront to close the deal on time, or walk away from the purchase of the home altogether one day prior to closing because the mortgage broker is unable to make any reduction in his/her fee after it has been disclosed to the borrower.

The primary flaw in the rule that is causing the harm illustrated above, as well as many other similar instances of harm to consumers, is the Federal Reserve Board's definition of the term "loan originator." The Board has defined "loan originator" to include mortgage broker businesses, as well as the individual loan originator employees working for those businesses. However, the Board has chosen to exempt mortgage lending businesses (*i.e.*, "creditors") from this definition, even though their individual loan originator employees are also covered by the definition of "loan originator" in the rule.

This disparity in the treatment of mortgage broker businesses and mortgage lending businesses has placed mortgage brokers at a considerable competitive disadvantage in relation to their competition in two primary respects. First, a mortgage broker is prohibited from ever adjusting its price, up or down, to benefit a consumer or secure a transaction, while a mortgage lender remains free to adjust its pricing for any reason as circumstances may warrant. Additionally, a mortgage broker is prohibited from compensating its employee loan originators on a commission basis, which remains the most economically viable means for a small business mortgage originator to compensate its individual loan officers.

NAMB continues to steadfastly believe that the Federal Reserve Board acted outside of the scope of its authority in regulating loan originator compensation in the manner prescribed in the rule. NAMB specifically takes issue with the Board's decision to arbitrarily sweep mortgage broker businesses into the rule's definition of "loan originator," over the objection of numerous industry leaders and contrary to the legislative intent of Congress, which crafted the original and proper definition of "loan originator" in the SAFE Act (12 U.S.C. 5101, et. seq.).

However, because the Board proceeded with implementation of its rule despite the concerns raised by industry leaders and members of Congress, and because multiple legal challenges to the rule have proven unsuccessful, NAMB believes it is now imperative for Congress to explore amending the Truth in Lending Act ("TILA") to limit the breadth of the negative impact of the Board's rule.

Specifically, NAMB believes TILA should be amended to include a definition of "loan originator" that mirrors the definition of "loan originator" found in the SAFE Act (12 U.S.C. 5101, et. seq.). The statutory definition of "loan originator" found in the SAFE Act should be carried throughout the framework of federal financial laws and regulations. Defining the same term differently in different statutes and regulations that affect the same industry and individuals only causes confusion and unnecessarily increases the costs and complexities of compliance. NAMB believes that specifically adding the definition of "loan originator" to the TILA statute and defining the term in the same manner as in the SAFE Act will help to clarify some of the confusion and controversy surrounding the Board's rule, and will also help bring a measure of even greater consistency to the federal regulation of our industry. NAMB also believes that the SAFE Act should be amended to provide state regulators with greater flexibility with regard to licensing loan originators.

IV. Consumer Financial Protection Bureau Proposals to Simplify Mortgage Disclosures

NAMB is very encouraged by the Consumer Financial Protection Bureau's ("CFPB") commitment to developing more consumer-friendly mortgage disclosures and the effort that is being made to solicit feedback on these forms from our industry.

Because buying a home is often one of the largest and most significant financial decisions in a person's life, NAMB believes it is critical to give consumers clear, easy-to-understand information that empowers them to compare mortgage products and providers and identify those that best meet their individual needs and goals.

Current mortgage disclosure forms are unnecessarily complex and entirely too difficult for most consumers to understand and use effectively. These forms are also redundant and therefore costly for originators to fill-out, which in turn increases the overall cost of obtaining a mortgage for consumers.

NAMB has specifically stressed the importance of removing the annual percentage rate ("APR") from any new mortgage disclosures that are developed, as most within our industry agree that the APR is extremely confusing and very difficult for borrowers to understand, even with the help of a knowledgeable loan originator. NAMB also believes that the sale price and estimated value of the property should be added to such disclosures, along with information about any mortgage insurance that that may be required in order to obtain the loan. In the end however, a truly consumer-friendly mortgage disclosure should help a borrower answer two basic questions: (1) can I afford this mortgage; and (2) can I find a better price or product elsewhere.

To date, the efforts being made by the CFPB to simplify consumer mortgage disclosures seem to be on track toward achieving a clearer more consumer-friendly set of forms. However, as the CFPB moves forward with testing and analyzing its draft forms, NAMB strongly encourages the CFPB to seek out and engage a qualified third-party verifier to conduct or monitor any consumer testing and assist in evaluating the results. As we have learned from prior efforts to review and revise consumer mortgage disclosures, relying on agency testing of agency-developed forms or procedures does not always yield the desired result, which is a better form for both consumers and the industry.

Because consumers ultimately bear the cost of implementation of any new disclosure form or procedure, NAMB believes it is imperative that the CFPB's new disclosures not only provide consumers with critical information in an easy-to-use format, but also that such disclosures are able to be implemented without further disruption to the industry or the home buying process.

V. Increase in Mortgage & Appraisal Fraud

Mortgage and appraisal fraud has been and continues to be a serious problem in our industry. Although recent studies have shown that instances of mortgage fraud are down as much as twenty-five percent (25%) from the peak numbers seen during the subprime and exotic loan boom between 2005 and 2007, a cloud continues to hang over our industry.

Industry self-policing and policy changes, such as enhanced employment verification at closing, additional credit report requirements, and authenticated IRS tax transcripts have served as an effective deterrent and detection mechanism for many types of fraud. However, with the historically high number of homeowners across the country who are in trouble with their mortgages, we have witnessed significant increases in fraudulent activity surrounding short sales, foreclosure rescue schemes, and some loan modification programs. Additionally, instances of appraisal fraud have more than doubled (from 16% of all fraud cases in 2006 to 33% of all cases since 2009) following implementation of the still highly controversial Home Valuation Code of Conduct ("HVCC"). Although the HVCC was designed to reduce the instances of fraud occurring in the appraisal process, it instead sparked significant turmoil, decreased competition in the appraisal industry, and eliminated virtually all checks and balances historically associated with home appraisals.

Critics of the HVCC maintain that appraisal management companies ("AMCs") offer only nominal compensation compared to what appraisers have traditionally been paid for their services, and this has led to more inexperienced appraisers who are unfamiliar with a particular area taking on appraisal assignments. It has also been suggested that AMCs are requiring appraisers to complete work in unrealistic time frames, which is resulting in sometimes fraudulent and often wildly inaccurate appraisal reports.

NAMB members have brought us countless examples of the specific hardships their customers have faced because of these and other issues surrounding the HVCC. Multiple members have reported that customers were unable to obtain the loan they applied for after an appraiser located fifty (50) miles or more away from the subject property and unfamiliar with the local market was selected by an AMC to provide the appraisal report; and because the appraisal process has made appraisers essentially anonymous, there are virtually no checks or balances and very little quality control that can be exercised in such situations.

Additionally, NAMB members across the country have shared with us examples of consumer appraisal costs that have risen between 120%-150% from pre-HVCC pricing. Before implementation of the HVCC, the average cost of a conventional single-family residential appraisal was roughly \$300-\$325 and an FHA appraisal typically cost the consumer between \$350-400. Now our members are seeing conventional single-family residential appraisals cost their customers \$425 or more and FHA appraisal costs are toping-out at or above \$500.

While consumer appraisal costs have risen substantially following implementation of the HVCC, we have also seen a dramatic decrease in appraiser compensation. It has become an unsettling trend to see borrowers pay in excess of \$450 for an appraisal, where the appraiser only earns half of that amount in compensation for his/her services, the rest being retained by the AMC responsible for hiring the appraiser. This particular financial arrangement is largely what has led to the increase in inexperienced appraisers being awarded more assignments, because the AMC will charge the borrower the same amount regardless of the skill or experience of the appraiser, but the AMC is able to compensate the appraiser based on his/her skill or experience.

The cumulative effect of all of this is that consumers are tending to pay significantly more money for lower quality appraisals, which in turn is making it more difficult, and sometimes impossible, for many consumers to obtain mortgage financing. Mortgage and appraisal fraud is jeopardizing the recovery of our housing market, causing countless problems for financial institutions and limiting opportunities for consumers. Moreover, because mortgage fraud is a crime that is often not vigorously investigated or prosecuted unless significant sums of money or large numbers of individuals are involved, NAMB believes that alternative enforcement mechanisms and other checks and balances need to be put into place. Specifically, NAMB believes that mortgage originators should not be permitted to own, in whole or in part, any AMC that the originator intends to or does in fact conduct business with.

VI. Qualified Mortgages ("QM") / Qualified Residential Mortgages ("QRM")

"Qualified mortgages" and "qualified residential mortgages" are mortgage loans with underwriting and product features that historical performance data suggests carry a lower risk of default (see chart above). As the rulemaking process for implementing the Dodd-Frank Act continues to move forward, these terms will be even more specifically defined.

NAMB believes that the definition of a "qualified mortgage" or "qualified residential mortgage" should include any fixed-rate mortgage with a term of ten (10) years or more, which is fully amortized and requires full documentation of the borrower's income and assets. NAMB does not believe it is necessary or appropriate for the Federal Reserve Board to be imposing debt-to-income or minimum credit criteria on these mortgages, particularly in light of the historical data showing how well these types of loans have generally performed. In fact, NAMB believes that this over-regulation is a prime example of the precise problem we highlighted earlier in our testimony. Rather than specifically identifying those mortgage products that were causing the vast majority of harm to consumers and to our mortgage and housing market and effectively removing those products from the shelves, the Board instead promulgated overly broad regulations that have failed to achieve their desired effect and have negatively impacted the origination of traditionally high-performing loans.

For this reason, NAMB strongly believes that "qualified mortgages" and "qualified residential mortgages" should be specifically exempt from the Board's discretionary regulatory authority under TILA. These mortgages, by definition, carry a lower risk of default based upon their features, terms and underwriting, and the Dodd-Frank Act already exempts "qualified residential mortgages" from risk-retention requirements.

By exempting "qualified residential mortgages" from the risk-retention requirements of the Dodd-Frank Act, the cost of securitizing these mortgages is reduced, thus providing a market incentive for the wide origination of responsible loans. NAMB believes this same principal is applicable in the case of rules enacted by the Board under its broad discretionary authority under TILA. Exempting "qualified mortgages" and "qualified residential mortgages" from onerous Board rules and regulations will further incentivize the origination of these responsible loans and will help ensure that these loans are less expensive for borrowers than other products carrying more risky features and less restrictive underwriting standards.

VII. Conclusion

NAMB and the mortgage professionals we represent nationwide are committed to strengthening our industry and serving and protecting our customers. However, we do not believe it is appropriate or even possible to legislate or regulate our way to an economic recovery.

We urge Congress and each of the federal financial regulatory agencies to pause from any efforts to promulgate or implement further changes or regulatory requirements on our industry for at least twenty-four (24) months. Allow our customers, our processes, and the market to catch-up to the numerous significant changes that have already taken effect, and at the same time, evaluate which of those changes may have gone too far and should be rolled-back in the interest of facilitating a swifter recovery.

NAMB appreciates all of the work that this Committee does on behalf of consumers and our industry, and we are particularly grateful for the opportunity to share our thoughts with you today on these issues that are of such great concern and importance all of us. Thank you for inviting NAMB to testify, and we look forward to continuing to work with you to find solutions to these issues that continue to delay our economic recovery and negatively affect consumers' ability to obtain affordable mortgage financing.

NCLR
NATIONAL COUNCIL OF LA RAZA

Commonsense Mortgage Origination Protections Empower Latino Homebuyers

Presented at

"Mortgage Origination: The Impact of Recent Changes on Homeowners and Businesses"

Submitted to

Subcommittee on Insurance, Housing, and Community Development
U.S. House of Representatives Committee on Financial Services

Submitted by

Janis Bowdler
Director, Wealth-Building Policy Project
National Council of La Raza

July 13, 2011

Raul Yzaguirre Building
1126 16th Street, NW, Suite 600
Washington, DC 20036

www.nclr.org

Good afternoon. My name is Janis Bowdler, and I am the Director of the Wealth-Building Policy Project at the National Council of La Raza (NCLR)—the largest national Hispanic* civil rights and advocacy organization in the United States. For the last four decades, NCLR has been committed to improving opportunities for the nation's 50.5 million Latinos. To this end, NCLR conducts research, policy analysis, and advocacy on a variety of financial services issues that affect the ability of Latinos to build and maintain assets and wealth. I would like to thank Chairwoman Judy Biggert and Ranking Member Luis Gutierrez for inviting me to participate in today's hearing.

For more than two decades, NCLR has engaged in public policy issues that focus on supporting strong fair housing and fair lending laws, increased access to financial services for low-income people, and promoting homeownership in the Latino community. And for more than ten years, the NCLR Homeownership Network (NHN)—a network of 50 community-based counseling providers—has been providing first-time homebuyers with the advice and guidance they need to navigate the mortgage process. NHN counselors have produced more than 25,000 first-time homebuyers over the last 13 years. NCLR's subsidiary, the Raza Development Fund (RDF), is the nation's largest Hispanic Community Development Financial Institution (CDFI). Since 1999, RDF has provided $500 million in financing to community-based development projects throughout the country, building the capacity of local nonprofits and creating opportunities for Latino communities. Our research, programs, and market investments have increased NCLR's institutional knowledge of how Latinos interact with the mortgage and financial markets and the impact on their communities.

NCLR strongly supports the Dodd-Frank Wall Street Reform and Consumer Protection Act. This landmark legislation includes new protections that will improve financial markets for Hispanic and immigrant consumers, a number of which will be under the jurisdiction of the newly created Consumer Financial Protection Bureau (CFPB). In addition, regulators are drafting rules that will guide the implementation of new remittance protections, underwriting standards, and mortgage reform. Though the majority of rules have yet to be finalized, NCLR has high hopes that the new rules will further the goals of Dodd-Frank by protecting consumers while maintaining market access.

In my brief comments today, I will draw your attention to three critical aspects of the mortgage origination process that are currently under consideration by Congress and federal regulators: the new Truth in Lending Act (TILA) disclosure being developed by CFPB; the Department of Housing and Urban Development's (HUD) Housing Counseling Program; and the Federal Reserve's pending rule to prohibit unfair steering practices.

Background

Homeownership has long been the primary asset for most Americans, steadily building modest wealth that can leverage education, entrepreneurship, or retirement opportunities. When nurtured over a lifecycle, home equity can be shared with the next generation and further their

* The terms "Hispanic" and "Latino" are used interchangeably by the U.S. Census Bureau and throughout this document to identify persons of Mexican, Puerto Rican, Cuban, Central and South American, Dominican, Spanish, and other Hispanic descent; they may be of any race.

financial security. Communities of color do not own homes at rates comparable to their White peers, which contributes heavily to the racial wealth gap.[*] Civil rights institutions have fought for decades for policies that ensure that qualified borrowers of color are able to access the same homeownership opportunities enjoyed by the rest of the market. Unfortunately, policies to this end have been undermined by lax oversight of financial institutions, faulty implementation, and predatory lending. An abundance of research has shown that Black and Hispanic borrowers were disproportionately sold subprime loans, even when their income and credit profiles warranted standard prime loans.[†] For this reason, NCLR testified before this committee in favor of many of the policies that were eventually included in Dodd-Frank.[‡]

There is overwhelming evidence demonstrating that minority borrowers pay more to access credit than similarly situated White borrowers. This pattern of overpayment, abuse, and discrimination disrupts the financial stability of low-income and minority communities, and impedes their upward mobility toward the middle class. The following is a summary of four critical barriers that NCLR identified prior to the passage of Dodd-Frank which characterized how the banking and financial services markets drain wealth rather than build it. These barriers demonstrate the need for improved regulatory systems, industry practices, and consumer supports.

- **Shopping for credit is nearly impossible.** Few shopping tools exist that can help borrowers create true apples-to-apples cost comparisons. As a result, some borrowers forgo shopping altogether while others rely on intermediaries, such as mortgage brokers or auto dealers, to shop on their behalf. Numerous studies and reports showing deception and hidden costs through these delivery channels demonstrate that brokers and dealers do not operate in a manner that truly benefits the borrower consistently.

- **Borrowers are steered toward expensive products regardless of creditworthiness.** Many low-income and minority borrowers have unique borrower profiles—such as thin credit files, multiple co-borrowers, or multiple sources of income—that are not easily processed through automated underwriting. Rather than taking the time to match these consumers with existing products that accurately measure their true risk, lenders would steer borrowers toward products that were easier to originate and highly profitable. Prior to Dodd-Frank, mortgage brokers and loan officers were paid kickbacks for putting consumers in loans with higher interest rates than their credit warrants.[§]

---

[*] The racial wealth gap leaves the average American family of color with only 16 cents for every dollar owned by the average White family. Wealth is what you own minus what you owe: assets minus debts. For more information, see Meizhu Lui, *Laying the Foundation for National Prosperity: The Imperative of Closing the Racial Wealth Gap* (Oakland, CA: Insight Center for Community Economic Development, 2009).

[†] Robert B. Avery, Kenneth P. Brevoort, and Glen Canner, "The 2007 HMDA Data," *Federal Reserve Bulletin* 94 (December 23, 2008); Debbie Gruenstein Bocian, Keith S. Ernst, and Wei Li, *Unfair Lending: The Effect of Race and Ethnicity on Price of Subprime Mortgages* (Durham, NC: Center for Responsible Lending, 2006).

[‡] Janet Murguía for the National Council of La Raza, *Laying the Foundation for Improved Access to Credit for Hispanic Families*, before the U.S. House of Representatives Committee on Financial Services, July 16, 2009, www.nclr.org/images/uploads/publications/RegReform_testimony_final.pdf (accessed July 2011).

[§] *Eliminating Systematic Charges on Home Loans: Fed Rules on Yield Spread Premiums* (Durham, NC: Center for Responsible Lending, 2010); Susan E. Woodward, *A Study of Closing Costs on FHA Mortgage*. Office of Policy Development and Research, U.S. Department of Housing and Urban Development. Washington, DC, 2008, www.urban.org/UploadedPDF/411682_fha_mortgages.pdf (accessed July 2011); and Keith Ernst, Debbie

- **Creditors trap borrowers in cycles of debt.** For some subprime borrowers, excessive fees, high interest rates, prepayment penalties, and mounting debt effectively trap them in the subprime market. For example, the pervasive use of loose underwriting criteria led to the origination of loans that homeowners could never afford to repay. The mortgage industry wagered that the value of home prices would continue to climb and clients would refinance if their mortgage product became too expensive. This practice led many families into a downward spiral of wealth-draining refinances that has contributed heavily to the current mortgage crisis.

- **Fraud and scams are rampant.** Compounding the impact of predatory lending and the gaps in consumer protections is the rise of fraud and scams targeting victims of burdensome debt and foreclosure. Research conducted by the Federal Trade Commission (FTC) shows that 14.3% of Hispanics are victims of fraud, compared to 6.4% of non-Hispanic Whites.* From fake credit cards claiming to help families build credit to foreclosure rescue scams claiming to help families save their home, fraud is on the rise.

Many have recognized the shortcomings of the mortgage system that led to the housing bubble and today's foreclosure disaster. The lack of transparency and accountability, as well as the increasing complexity of mortgage products made it difficult for even the most diligent borrower to shop effectively. In such an environment, deceptive actors had their way at the expense of responsible lenders, homeowners, and taxpayers. The protections established in Dodd-Frank respond directly to this situation. Implemented properly, the regulations should advance a mortgage market that works more fairly for all.

Empowering Homebuyers at Origination

Homeownership stakeholders must work together to ensure that the mortgage market treats consumers and honest dealers fairly and maintains a responsible flow of credit to qualified borrowers. Dodd-Frank established new provisions intended to further this goal. However, final regulations must be drafted and implemented before reform is fully realized. NCLR plans to submit public comment on key proposed rules, and we encourage others to leverage the rulemaking process to help refine final regulation. In response to questions raised during this hearing, we offer our perspective on three elements of origination currently under public debate.

Revised TILA Disclosure
One of the most daunting challenges for homebuyers, especially those new to the process, is comparing loan terms and offers. The Good Faith Estimate (GFE) was intended as a shopping tool that would allow borrowers to determine which loan made sense for their personal circumstances. Several challenges made the GFE less effective than intended. NHN housing counselors point out that the GFE is frequently delayed, sometimes during closing, and comes too late in the process to inform borrower decision-making. Similarly, the TILA disclosure is

---

Gruenstein Bocian, and Wei Li, *Steered Wrong: Brokers, Borrowers, and Subprime Loans* (Durham, NC: Center for Responsible Lending, 2008), www.responsiblelending.org/mortgage-lending/research-analysis/steered-wrong-brokers-borrowers-and-subprime-loans.pdf (accessed July 2011).
* Federal Trade Commission, *Consumer Fraud in the United States: An FTC Survey*. Washington, DC, 2004.

given at the time of closing when few borrowers are in a position to walk away from the deal. Both forms have been criticized for giving too little or too much information, causing confusion, and being burdensome for lenders. For these reasons, Dodd-Frank requires the two forms to be combined, revised, and given to borrowers three days after they have submitted a mortgage application.

NCLR applauds the CFPB for its progress so far in developing and evaluating a revised GSE/TILA disclosure. The online feedback tool is transparent and makes it simple for a broad audience to provide input on the design and content. NCLR distributed the link to NHN organizations and encouraged them to share their critiques as experts working with first-time homebuyers. According to the CFPB website, more than 13,000 comments were submitted during the first round. In addition to the innovative comment process, CFPB co-developed its Spanish-language version of the disclosure. Word-for-word translations are often problematic and fail to effectively communicate the same meaning, tone, and purpose as the original English. Rather than a strict translation, best practice calls for applying the same creative thinking used to develop plain English to draft terms and phrases in Spanish. Using such a process will help CFPB create a document that is culturally relevant, easy to understand, and user-friendly. We urge CFPB to use the online comment tool to solicit comments on the Spanish version of the disclosure as well.

The TILA disclosure is not a substitute for responsible underwriting by lenders. However, a well-written disclosure can be an important tool to help borrowers understand the terms of their loan. CFPB staff are wise to undergo a thorough drafting and testing process before publishing a final version for public comment. It is our understanding that additional rounds of edits and testing are forthcoming. We look forward to participating in this process and offering additional comments and feedback.

Prepurchase Housing Counseling

The Housing Counseling Assistance Program administered by the Department of Housing and Urban Development (HUD) was established in 1968. Early on, the program focused on Federal Housing Agency (FHA) mortgage insurance borrowers, however, over time the scope of the program has broadened to focus on providing education and advice to first-time homebuyers. Over the last decade, the Housing Counseling Assistance Program has adapted to a dynamic housing market by increasing its capacity and sophistication. Today, many housing counselors have mortgage origination experience and provide objective information, advice, and guidance to homebuyers.

Prepurchase programs are delivered before individuals become homeowners, and focus on assisting prospective homeowners to qualify for a mortgage, apply successfully, and succeed as homeowners. Indeed, research has shown that borrowers who receive prepurchase counseling are less likely to default than their peers.* During the bubble years of 2004–2007, housing

* Chris Herbert for the Joint Center for Housing Studies of Harvard University, "Housing Counseling: Past and Future Trends" (presented at Housing Counseling Intervention: Research and Impact briefing, June 21, 2010), www.995hope.org/press-media/related-research-and-downloads/Mortgage-Counseling-Benefits-Validated (accessed July 2011).

counselors often competed with realtors, lenders, and loan brokers offering unrealistic loans, many of which were outright predatory. Housing counselors had the less popular job of instructing clients on the steps necessary to enter safely into homeownership—steps that were often seen by originators as a roadblock to a fast and lucrative closing.

Precisely because housing counseling has been so effective, Congress's elimination of funding for the annual allocation for HUD's Housing Counseling Assistance Program represents a huge loss for homebuyers and for communities of color in particular. Homebuyers already struggling to beat out cash-laden speculators for properties in their own neighborhoods will find themselves even more imperiled absent a counseling infrastructure that can aid in the transaction. Moreover, at a time when most federal efforts to curb foreclosure rates have fallen far short of their goals, the HUD Housing Counseling Assistance Program has stood out as an efficient use of resources. Last year, certified housing counseling agencies helped 469,484 clients who were delinquent on their mortgages successfully avoid foreclosure, preventing approximately $28 billion in damage to the economy and reducing lender losses.

Experience shows that the loss of community-based counseling services will leave a void that is likely to be filled by scam artists. Unscrupulous activity will continue to be particularly acute in communities of color, where predatory practices have been in play for decades. Rather than ax the program, Congress and HUD should look for ways to integrate prepurchase counseling into the origination process. Federal funding has never been intended to be the sole source of support for the counseling program. However, without the infrastructure created by HUD, the counseling field will be unable to maintain its depth and capacity. Truly, the HUD Housing Counseling Assistance Program is an excellent example of an effective and highly functional public-private partnership. NCLR urges Congress to fully fund the program at $88 million in the 2012 budget.

Preventing Unfair and Deceptive Steering

The misalignment of incentives at the origination level was a primary cause of the housing bubble. Simply put, brokers and originators were paid more for steering creditworthy borrowers into expensive loans with risky terms such as high upfront fees, interest-only payments, negative amortization, and exploding interest rate adjustments. This practice was especially common among Latino borrowers, as described in the background section above. To address this issue, the Federal Reserve solicited public comment on a proposed rule, which was the product of years of study, public hearings, and earlier rulemaking.* Dodd-Frank supported the direction of the Federal Reserve by incorporating two provisions—a duty of care for mortgage originators and prohibitions on compensation-based incentives to steer—that closely track the Federal Reserve's proposed rule.

Steering was one of the most egregious deceptive lending tactics employed against Hispanic borrowers. Therefore, we strongly support the commonsense regulations proposed by the Federal Reserve, further cemented by Dodd-Frank. The proposed rule rightly prohibits compensation based on the terms of the loan, excluding principal, as well as other protections.

* Janis Bowdler for the National Council of La Raza, *The Impact of the Home Equity Lending Market on Latino Consumers*, before the Board of Governors of the Federal Reserve System, August, 15, 2006.

The rule does not eliminate the ability of originators to be paid for their work to package and close a mortgage loan.

Mortgage brokers play an essential role in helping Latino families purchase their homes, especially when Spanish is their preferred language. Like housing counselors, many brokers use a one-on-one style that appeals to consumers making such a critical and confusing decision. Unfortunately, this trust was not honored by many unscrupulous brokers, causing irreparable harm to families and honest brokers.* In fact, the harm done by deceptive brokers and the inability of banks to control the delivery channel is one reason why lenders have all but eliminated their wholesale units. The steps taken by the Federal Reserve are reasonable and will help to restore trust and confidence in the system. We support the full implementation of the final rule. In addition, as the CFPB assumes oversight, we encourage the Federal Reserve to work closely with them to harmonize their work. Such opportunities lay in the development of the new mortgage disclosure forms and the proposed rule on Qualified Residential Mortgage (QRM) and Qualified Mortgage (QM). Furthermore, we recommend strict oversight of other mortgage fees to protect consumers from absorbing potential cost-shifting on the part of mortgage lenders, and full disclosure of all associated fees.

Conclusion

In sum, NCLR supports the mandates of Dodd-Frank that further a responsible and accessible mortgage market that rewards honest lenders and aids qualified homebuyers and homeowners. In our testimony, we offered three modest recommendations: make the Spanish TILA disclosure available for public comment via CFPB's online feedback tool; fund the HUD Housing Counseling Assistance Program at $88 million; and implement the Federal Reserve's rule on steering as well as protections for borrowers from potential cost-shifting fees.

* Janis Bowdler and Timothy Sandos, *Saving Homes, Saving Communities: Latino Brokers Speak Out on Hispanic Homeownership* (San Diego, CA: National Association of Hispanic Real Estate Professionals/Washington, DC: National Council of La Raza, 2007), www.nclr.org/index.php/publications/saving_homes_saving_communities_latino_brokers_speak_out_on_hispanic_homeownership (accessed July 2011).

For release on delivery
2:00 p.m. EDT
July 13, 2011

Statement of

Sandra F. Braunstein

Director, Division of Consumer and Community Affairs

Board of Governors of the Federal Reserve System

before the

Subcommittee on Insurance, Housing, and Community Opportunity

Committee on Financial Services

U. S. House of Representatives

Washington, D.C.

July 13, 2011

Introduction

Chairwoman Biggert, Ranking Member Gutierrez, and Members of the Subcommittee, I appreciate the opportunity to appear today to discuss regulatory actions taken by the Federal Reserve Board to address the recent challenges in the home mortgage market and to enhance consumer protections for homeowners. The Federal Reserve is committed to promoting sustainable homeownership through responsible mortgage lending. While the expansion of the subprime mortgage market increased consumers' access to credit, homeowners and communities suffered from lax underwriting standards and other unfair or deceptive practices that resulted in unsustainable loans.

Over the past three years, the Board has engaged in a series of rulemakings designed to reform mortgage lending. In addition to direct consumer benefits, protecting borrowers with responsible underwriting standards and other regulatory reforms can provide a broader benefit by enhancing the integrity, consistency, and proper functioning of the mortgage market and, thereby, increasing investor confidence. The Federal Reserve's goal has been to craft clear rules that deter abuses while preserving the ability of responsible lenders to meet the needs of all segments of the market, including traditionally underserved borrowers and communities.

Specifically, during this time, the Board comprehensively addressed the need for mortgage reform by issuing seven final rules under the Truth in Lending Act (TILA) and Home Ownership and Equity Protection Act (HOEPA) plus five additional proposed rules that will become the responsibility of the Consumer Financial Protection Bureau (the Bureau). These 12 rulemakings cover all stages of the mortgage lending process, including pre-application advertising, loan origination, appraisals, underwriting, disclosures, loan servicing, and assignment of the loan to investors. In my testimony today, I will first summarize the Board's rules to expand the substantive protections for consumer mortgage transactions. I will then discuss the Board's efforts to improve mortgage disclosures and the status of those proposals in light of the upcoming transfer of authority to the Bureau.

I. The Board's Efforts to Expand Substantive Protections for Consumer Mortgages

A. The 2008 HOEPA Rulemaking

Following a series of public hearings, extensive research, and outreach to consumer groups, industry representatives, and other state and federal agencies, in July 2008, the Board used its authority under TILA and HOEPA to issue final rules establishing sweeping new regulatory protections for consumers in the residential mortgage market. Importantly, these rules apply to all mortgage lenders, not just depository institutions supervised by the federal banking and thrift agencies.

In response to specific problems we saw in the subprime market, some restrictions in the final rules apply only to higher-priced mortgage loans. Other provisions, however, apply to all mortgage loans secured by a consumer's principal dwelling. In addition to rules that protect consumers from unfair or abusive lending and mortgage-servicing practices, these rules also govern mortgage advertisements to ensure they provide accurate and balanced information and do not contain misleading or deceptive representations. Another component of the final rules ensures that for all types of mortgage loans, consumers receive transaction-specific cost disclosures early enough to use while shopping for credit.

1. Protections for Higher-Priced Mortgage Loans

The Board's HOEPA rules added four key protections for a newly defined category of "higher-priced mortgage loans." These loans are defined as consumer-purpose loans secured by a consumer's principal dwelling and having an annual percentage rate (APR) that exceeds the average prime offer rate for comparable transactions by at least 1-1/2 percentage points for first-lien loans, or 3-1/2 percentage points for subordinate lien loans.[1]

These four protections for higher-priced mortgage loans are as follows:

Underwriting Requirements. The July 2008 rules prohibit lenders from making any higher-priced mortgage loan without regard to the borrower's ability to repay the obligation from income and assets other than the home. First, lenders are prohibited from making "stated income" loans. Lenders are required in each case to verify the income and assets they rely upon to determine the borrower's repayment ability. Lenders also must consider and verify the borrower's other debt obligations, such as through the use of a credit report. The final rule is intended to ensure that creditors do not assess repayment ability using overstated incomes or understated payment obligations. The rule is sufficiently flexible to allow lenders to adapt their underwriting process to accommodate a borrower's particular circumstances, such as when the borrower is self-employed.

Second, lenders are presumed to comply with the ability-to-pay requirement only if they take into account the highest scheduled payment in the first seven years of the loan, rather than the consumer's initial monthly payment. For example, for an adjustable rate mortgage (ARM) with a discounted initial interest rate that is fixed for the first five years, the lender determines repayment ability using the scheduled payment in the sixth and seventh years, which is based on the fully indexed rate.

---

[1] The Board derives the average prime offer rates from Freddie Mac's Primary Mortgage Market Survey and publishes these rates on a weekly basis. Based on the available data, the "higher-priced" thresholds adopted by the Board are intended to cover all, or virtually all, of the subprime market.

I should note that the underwriting requirements legislated in the 2010 Dodd-Frank Wall Street Reform and Consumer Protection Act (the Dodd-Frank Act), which apply to all mortgage loans, are substantially similar, but not identical to the ability-to-repay requirements adopted by the Board in 2008 for higher-priced mortgage loans. I will discuss the Board's proposal to implement the Dodd-Frank Act "ability-to-repay" provisions later in my testimony.

Restrictions on Prepayment Penalties. Prepayment penalties can prevent borrowers from refinancing their loans to avoid monthly payment increases or if their loan becomes unaffordable for other reasons. Under the final rules, prepayment penalties are prohibited if the loan's monthly payment can change during the initial four years after consummation. For other higher-priced loans, a prepayment penalty cannot last for more than two years.

Escrow Accounts. The Board's July 2008 rules also require creditors to establish an escrow account for property taxes and homeowner's insurance for all first-lien mortgage loans above the higher-priced threshold. This addresses the concern that the absence of escrows in the subprime market increases the risk that consumers' borrowing decisions will be based on misleading low payment quotes that do not reflect the true cost of their homeownership obligations. The rule preserves consumer choice by permitting creditors to allow consumers to opt out of the escrow account after 12 months. Subsequently, the Dodd-Frank Act codified the final rules' requirement for establishing escrow accounts, with some modifications and additions. The Dodd-Frank Act escrow provisions are the subject of a proposed rulemaking, which I will describe later in my testimony.

2. Protections for All Loans Secured by a Consumer's Principal Dwelling

In addition to the rules for higher-priced loans, the July 2008 final rules adopted the following protections that apply to all mortgage loans secured by a consumer's principal dwelling.

Appraisal Independence. The final rules include provisions designed to protect the integrity of the appraisal process. These rules seek to ensure that real estate appraisers are free to use their independent professional judgment in assigning home values. Accordingly, the Board's rules prohibit lenders or brokers from coercing, influencing, or otherwise encouraging an appraiser to misstate or misrepresent the value of the property. The rules also prohibit a creditor from extending credit when the creditor has reason to know that the appraiser was encouraged to misstate or misrepresent the value of the dwelling, unless the creditor determines that the appraisal was accurate, or the creditor bases its decision on a separate appraisal that is untainted by coercion.

Subsequently, the Dodd-Frank Act codified the anti-coercion provisions in the Board's rules, with some modifications and additions, including a provision requiring that independent appraisers receive customary and reasonable compensation for their services. The Board implemented these provisions of the Dodd-Frank Act in an interim final rule, which I will discuss later in more detail.

Unfair Loan Servicing Practices. The Board also prohibited loan servicers from engaging in certain unfair billing practices. Specifically, the final rules prohibit servicers from failing to credit a payment to a consumer's account as of the date received. The rules also prohibit the "pyramiding" of late fees. Under the rules, servicers may not impose a late fee on a consumer when the consumer's payment was timely and made in full except for its failure to include a previously assessed late fee. In addition, the rules prohibit loan servicers from failing to provide a loan payoff statement on a timely basis after receiving a request from the consumer or any person acting on the consumer's behalf.

Advertising Rules. The final rules also seek to ensure that mortgage loan advertisements do not contain misleading or deceptive representations. Thus, the rules require that advertisements for both closed-end loans and home equity lines of credit (HELOCs) provide accurate and balanced information about rates, monthly payments, and other features in a clear and conspicuous manner. In addition, the Board used its authority under HOEPA to prohibit several deceptive or misleading advertising practices in advertisements for closed-end mortgage loans.[2] For example, an advertisement for a variable rate loan may not use the word "fixed" in referring to the interest rate or payment unless the advertisement includes an equally prominent statement of the time period for which the rate or payment is fixed. The rules also prohibit misrepresentations about government endorsement of the loan program and misleading claims of "debt elimination."

Earlier Cost Disclosures. To assist consumers in navigating today's complex market for mortgage products, the final rules require lenders to provide consumers with transaction-specific cost disclosures earlier in the application process, so that they can be used by consumers while shopping for a mortgage loan. Under the July 2008 rules, creditors must provide a good faith estimate of the loan costs and scheduled payments within three days after the creditor receives the consumer's application. The rule applies to any closed-end home-secured loan, including

[2] In September 2010, the Board proposed to apply these same prohibitions to advertisements for HELOCs.

home refinance loans and home-equity loans. (Previously, early cost estimates were required only for home-purchase loans.) To ensure that consumers are able to use the information when comparing mortgage loans, consumers cannot be charged any fee until after they receive the early disclosures, except a reasonable fee for obtaining the consumer's credit history.[3]

B. The Board's Rules on Loan Originator Compensation

In September 2010, the Board issued a final rule regulating mortgage originator compensation practices to fulfill its responsibility under HOEPA to prohibit practices in connection with mortgage loans that the Board finds to be unfair or deceptive. The effective date of the rule was delayed until April 2011 to provide sufficient time for creditors and loan originators to make the necessary adjustments to their compensation agreements and practices.

The final rule addresses the two basic ways in which originator compensation is paid. In so-called "creditor-pay" transactions, the lender makes a payment to the loan originator, which is funded by the consumer's payment of a higher interest rate. In the second model, called "consumer-pay" transactions, the consumer pays the loan originator directly, either from existing funds or from the loan proceeds. The final rule regulates the manner in which loan originators may be compensated, but not the amount. The rule has three major components.

First, with respect to "creditor-pay" transactions, the Board's rule prohibits loan originators from receiving compensation in an amount "that is based on any of the transaction's terms or conditions," except the amount of credit extended. This rule applies to loan originator compensation that is paid by a bank or other creditor to its loan officer employees as well as to

[3] In July 2008, the Congress enacted the Housing and Economic Recovery Act of 2008, which included the Mortgage Disclosure Improvement Act (MDIA). The MDIA codified the Board's new requirements for providing earlier TILA disclosures within three days after application and also added some additional requirements, including a requirement that these early cost estimates be provided at least seven days before the loan closing. The Board issued final rules implementing the MDIA in May 2009.

compensation paid by the creditor to a mortgage broker. This portion of the rule is designed to address the concern that loan originators who are paid out of the interest rate in the form of a "yield spread premium" have a conflict of interest in their dealings with consumers because originators have a personal incentive to offer the consumer an interest rate that is higher than the best rate for which the consumer qualified. Under the rule, consumers still have the option of funding their upfront closing costs, including originator compensation, through a higher interest rate, as long as the amount of originator compensation does not vary based on the rate or other loan terms.

Second, for consumer-pay transactions, the final rule states that if the consumer directly compensates a loan originator, compensation may not be paid to a loan originator by any other person in connection with the transaction. This provision addresses the problem that loan originators were frequently compensated by both the consumer and the creditor in a manner that was not transparent to consumers and that could lead consumers to believe, wrongly, that by paying a loan originator directly, the loan originator would work on their behalf to find the most favorable loan. One consequence of this prohibition is that in consumer-pay transactions, a mortgage brokerage firm that is paid directly by the consumer may not pay a commission specific to that transaction to its loan officer.[4] Because the restriction only covers payments that are specific to the particular transaction, a brokerage firm that is paid by the consumer directly

[4] The Board believed it was necessary to prohibit a brokerage firm from sharing the consumer-paid compensation with its loan officer to prevent the loan officer from influencing whether the firm's compensation will be paid by the creditor or directly by the consumer and, therefore, potentially steering consumers to more expensive transactions. This could occur because in a "creditor-pay" transaction, the loan originator cannot be paid on the basis of the loan's rate or other terms (except the amount of the loan), so the amount of compensation the loan originator may receive is fixed in advance and not negotiated with the consumer. However, this limitation does not apply in a "consumer-pay" transaction, where a loan originator can negotiate any compensation amount that the consumer will accept. Under the Board's rule a loan officer does not receive a portion of the compensation paid directly by the consumer, which eliminates the incentive for steering consumers to a "consumer-pay" loan that is more expensive.

can still provide its loan officers with incentive compensation (in addition to salaries or hourly wages) without violating the rule.[5]

Finally, the final rule prohibits loan originators from "steering" consumers to consummate a transaction with a particular creditor based on the fact that the loan originator will receive greater compensation from that creditor. This provision responds to concerns that in creditor-pay transactions, a mortgage broker who works with a number of creditors could influence the consumer to consummate a loan with the creditor whose compensation of the loan originator is highest, even though the loan carries a higher interest rate and is not in the consumer's interest. Thus, this aspect of the final rule applies only in creditor-pay transactions.

In March 2011, two lawsuits were filed by trade associations representing mortgage brokers challenging the Board's September 2010 final rule on loan originator compensation. Brokers' representatives asserted that the Board should not have issued final rules but should have instead allowed the Bureau to address the issue of loan originator compensation in a future rulemaking under the Dodd-Frank Act. The brokers also asserted that consumer disclosures should be sufficient to allow consumers to make informed decisions and that substantive restrictions are not needed. Both lawsuits have been dismissed, and compliance with the Board's rules has been mandatory since April.

The Board issued the September 2010 final rules after giving much consideration to various alternatives. Concerns had been raised during the mortgage crisis that some consumers obtained unaffordable loans that carried interest rates that were higher than the best rate for which they qualified. In response to increasing mortgage defaults, in 2007 the Board held

---

[5] For example, a brokerage firm could pay bonuses to loan officers who exceed a threshold number of loans within a specified period.

hearings and solicited public comments on how the Board might use its rulemaking authority to prevent abuses in the subprime lending market while still preserving responsible lending. Commenters raised concerns about the fairness and transparency of creditors' practice of compensating brokers out of the yield spread premium. These commenters noted that consumers generally are not aware of these payments from creditors to brokers, or that such payments increase consumers' interest rates. Commenters also stated that consumers may mistakenly believe that a broker seeks to obtain the best interest rate available for them.

To address the heightened concerns regarding the conflict of interest presented by mortgage broker compensation, in January 2008, the Board proposed a rule that would require mortgage brokers to disclose clearly and conspicuously to consumers their total compensation (including any portion paid by the creditor as a "yield spread premium") before obtaining the consumer's written agreement. Brokers would also have to disclose that a creditor payment to the broker could influence the broker to offer the consumer loan terms that would not be in the consumer's interest or were not the most favorable terms the consumer could obtain. Representatives of mortgage brokers opposed this disclosure proposal.[6] Brokers also opposed disclosures concerning loan originator compensation that were adopted by the Department of Housing and Urban Development (HUD) in 2008 under the Real Estate Settlement Procedures Act (RESPA).

Based on the results of consumer testing and other information, the Board declined to adopt the proposed disclosures for mortgage broker compensation when the Board issued the July 2008 final rules under HOEPA. The Board had anticipated that the proposed disclosures

[6] One of the arguments made by the brokers was that the Board should not mandate TILA disclosures concerning the loan originator's compensation in a consumer credit transaction unless the Board is also able to mandate that creditors disclose to consumers the amount the creditor will earn if it sells the loan to a secondary market investor.

would increase transparency and increase competition in the market for brokerage services. However, the results of the Board's one-on-one interviews with consumers suggested that the proposed agreement and disclosures would confuse consumers and undermine their decision making rather than improve it.

Concluding that disclosures alone would not be sufficient to allow consumers to avoid unfair practices related to loan originator compensation, in August 2009, the Board proposed to use its authority under HOEPA to adopt substantive rules that would prohibit certain originator compensation practices that the Board found to be unfair. The September 2010 final rules on originator compensation are substantially similar to the Board's August 2009 proposal.

In issuing the final rules, the Board considered the recently enacted provisions in Section 1403 of the Dodd-Frank Act, which address the same concerns. The Board believed that the rules it proposed in August 2009 were consistent with the provisions in the Dodd-Frank Act. The Board recognized, however, that there were some differences and that, as drafted, the Board's proposal would not fully implement the provisions in Section 1403. Changes to the Board's proposal to implement Section 1403 would have called for the issuance of a new proposed rulemaking.[7] The Board determined the best way to effectuate Section 1403's legislative purpose and eliminate, without further delay, the unfair practices that the Congress sought to prohibit was to finalize the 2009 proposal. Going forward, the Bureau will be responsible for issuing rules that fully implement the loan originator provisions in Section 1403.

[7] The Board's 2009 proposal and the final rules were based on the Board's authority under TILA to prohibit unfair or deceptive practices in connection with mortgages. The prohibitions in Section 1403 are intended to be implemented without the need for findings under the "unfair or deceptive" standard that applied to the Board's rulemaking.

C. Rules Implementing Title XIV of the Dodd-Frank Act

Title XIV of the Dodd-Frank Act constitutes the "Mortgage Reform and Anti-Predatory Lending Act." Among other things, Title XIV amends TILA to establish minimum underwriting standards to implement the statute's requirement that creditors determine that the consumer has a reasonable ability to repay the loan according to its terms. Title XIV also imposes new requirements for loan originators, high-cost mortgages, escrow accounts, and residential real estate appraisals.

The Board's general rulemaking authority under TILA will transfer to the Bureau on the designated transfer date, which is July 21, 2011. Prior to that date, the Board continues to be responsible for implementing TILA, including the amendments made by Title XIV of the Dodd-Frank Act. Accordingly, following enactment of the Dodd-Frank Act, the Board has continued to fulfill its statutory responsibilities under TILA by issuing regulatory proposals to implement the provisions in Title XIV.

1. Appraisal Independence

Independent and credible real estate valuations are critical to prudent residential mortgage lending. The information that appraisals provide on a property's market value also assists consumers in making informed borrowing decisions. Thus, federal banking regulators have stressed to financial institutions the importance of quality appraisals and an independent appraisal process. Federal banking agencies initially adopted prudential appraisal regulations for the institutions they supervise in 1990, and subsequently issued supervisory guidance clarifying the agencies' expectations for institutions' appraisal process.[8]

The most recent supervisory guidance, issued by the agencies in 2010, reflects recent changes in industry appraisal practices including lenders' increased use of third-party appraisal management companies (AMCs). These guidelines remind financial institutions that, if a third party performs all or part of their appraisal function, the institutions remain responsible for ensuring that the third party complies with all applicable laws and regulations.

As I discussed earlier, in July 2008, the Board issued final rules to strengthen the valuation process. These rules prohibited coercion of appraisers by creditors, mortgage brokers, and their affiliates. Subsequently, the Dodd-Frank Act codified the anti-coercion provisions in the Board's July 2008 final rules, while also making some modifications and additions, including a provision requiring that independent appraisers receive customary and reasonable compensation for their services. The Dodd-Frank Act directed the Board to issue interim final rules to implement the act's appraisal independence provisions within 90 days after enactment.

Consistent with this mandate, in October 2010, the Board issued for public comment interim final rules on appraisal independence. These interim final rules include several provisions that protect the integrity of the appraisal process. As with the Board's 2008 final rules, the interim final rules prohibit coercion and other similar actions designed to cause appraisers to base the appraised value of properties on factors other than their independent judgment. For example, they prohibit a party from withholding or threatening to withhold timely

[8] The 1990 prudential appraisal regulations were developed by the Federal Financial Institutions Examination Council pursuant to Title XI of the Financial Institutions Reform, Recovery, and Enforcement Act of 1989. These regulations applied to institutions supervised by the Federal Reserve Board, the Federal Deposit Insurance Corporation, the National Credit Union Administration, the Office of the Comptroller of the Currency, and the Office of Thrift Supervision.

payment from a person that prepares an appraisal because the person did not value the consumer's principal dwelling at or above a certain amount.

The 2010 interim final rules also prohibit appraisers and appraisal management companies from having a financial or other interest in the property or the credit transaction that is the subject of the appraisal. To facilitate compliance, the interim final rules provide a "safe harbor" for creditors that observe certain restrictions on the selection, supervision, and compensation of appraisers. Under the interim final rules, a creditor or settlement service provider that has information about material misconduct by an appraiser must file a report with the appropriate state licensing authorities.

To protect the quality of appraisals, the Dodd-Frank Act also requires that a creditor and its agent pay an independent "fee appraiser" at a rate that is that is customary and reasonable for the geographic market where the property is located. To implement this provision, the interim final rules do not establish a minimum fee schedule, but instead provide two alternative methods that creditors or their agents may use to establish an appropriate fee. First, a creditor and its agent are presumed to comply if the fee amount paid to the appraiser is reasonably related to the recent rates paid for appraisal services in the relevant geographic market and the creditor or agent has adjusted the recent rate after taking into account specified factors, such as the type of property, the scope of work, and the appraiser's qualifications and experience.[9]

Second, a creditor or its agent is also presumed to comply if it determines the fee by relying on third-party information, such as a government agency fee schedule, an academic study, or an independent private-sector survey. Consistent with the Dodd-Frank Act's

[9] In addition, to qualify for this presumption the creditor must not have engaged in any anti-competitive actions in violation of state or federal law that affect the appraisal fee, such as price-fixing or restricting others from entering the market.

requirements, third-party surveys and similar studies must not include fees paid to appraisers by appraisal management companies.

Compliance with the interim final rules on appraisal independence became mandatory on April 1, 2011. Thus, the rules have only been in effect for a little more than 90 days. During this time, some fee appraisers have reported that the fees offered by appraisal management companies have not increased as they had expected, and therefore, they express concern about whether appraisal management companies are complying with the "customary and reasonable" fee requirement. However, such determinations must be made case-by-case, based on the particular facts and circumstances. The Board has and will continue to review such complaints for the institutions it supervises, while forwarding complaints about other institutions to the appropriate federal or state agency.

Going forward, the Board and the other federal banking agencies, the Federal Housing Finance Agency, and the Bureau, will share responsibility for jointly issuing permanent rules on appraisal independence. In developing permanent rules, we will consider the public comments received on the October 2010 interim final rules as well as the experience we have gained through the examination process and the handling of the complaints we have received since the interim rules became effective.

2. Escrow Accounts

As discussed previously, in July 2008, the Board issued final rules requiring creditors to establish an escrow account for property taxes and homeowner's insurance for all higher-priced first-lien mortgage loans. This requirement addresses the concern that the absence of escrows in the subprime market increases the risk that consumers' borrowing decisions will be based on misleading low payment quotes that do not reflect the true cost of their homeownership obligations. Under these rules, a creditor may allow consumers to opt out of the escrow account after 12 months.

In March 2011, the Board issued a final rule to implement a provision of the Dodd-Frank Act that increased the annual percentage rate (APR) threshold used to determine whether a mortgage lender is required to establish an escrow account for "jumbo" mortgage loans. Jumbo loans are loans that exceed the conforming loan-size limit for purchase by Freddie Mac, as specified by the legislation. Under the July 2008 final rules, a first-lien mortgage loan is considered a higher-priced mortgage loan if its APR is 1-1/2 percentage points or more above the current average prime offer rate. As amended by the Dodd-Frank Act, the escrow requirement applies to first-lien jumbo loans only if the loan's APR is 2-1/2 percentage points or more above the average prime offer rate. The March 2011 final rule became effective on April 1, 2011.

Also in March 2011, the Board published proposed rules to implement changes to the escrow account requirement that are mandated by the Dodd-Frank Act. The proposed rules would expand the minimum period for mandatory escrow accounts from one to five years and, under certain circumstances, such as when the consumer is delinquent or in default, for a longer period of time. In addition, the proposal would establish two new disclosures relating to escrow accounts. One disclosure would be required three business days before consummation of a mortgage transaction for which an escrow account will be established. This disclosure would explain, among other things, what an escrow account is and how it works, and would state the risk of not having an escrow account. The Dodd-Frank Act requires such a disclosure for higher-priced mortgage loans that have mandatory escrow accounts, but the Board proposed to require the same disclosure for all mortgage loans that have escrow accounts.

The second disclosure would be given to consumers before a mortgage transaction is consummated without an escrow account or before an escrow account on an existing mortgage loan will be cancelled. This disclosure would explain escrow accounts, the risk of not having an escrow account, and the potential consequences of failing to pay home-related costs, such as taxes and insurance, in the absence of an escrow account.

Under the Dodd-Frank Act, the Board is authorized to exempt certain creditors from the escrow requirements if they operate predominantly in rural or underserved areas and originate a limited number of loans that they hold in portfolio. Creditors would be eligible for the exemption if they annually originate and retain the servicing rights to 100 or fewer loans and do not otherwise maintain escrow accounts for the mortgage loans they service. The proposed rule seeks to exempt creditors that meet the statutory criteria and that cannot cost-effectively establish escrow accounts. The exemption would permit these creditors to continue offering mortgage credit to consumers rather than leave the higher-priced loan market. Consistent with the exemption's purpose, the proposed rule would limit the definition of "rural" to those areas most likely to have only limited sources of mortgage credit.

3. Dodd-Frank Act Requirements on Ability-to-Repay

In April 2011, the Board published for public comment proposed rules that would implement provisions of the Dodd-Frank Act that seek to strengthen mortgage underwriting procedures. The statute requires a creditor to make a reasonable and good faith determination that the consumer will have a reasonable ability to make the mortgage payments, including any mortgage-related obligations (such as property taxes). The Board's existing rules prohibit a creditor from making a higher-priced mortgage loan without regard to the consumer's ability to make the loan payments from income or assets other than the home. The Dodd-Frank Act expands the ability-to-repay requirement to cover any consumer credit transaction secured by a dwelling regardless of how the loan is priced (excluding open-end credit plans, timeshare plans, reverse mortgages, and temporary loans).

Consistent with the act, the Board's proposed rule would provide four options for complying with the ability-to-repay requirement. First, a creditor can meet the general ability-to-repay standard by considering and verifying specified underwriting factors, such as the consumer's income or assets. Second, a creditor can make a "qualified mortgage," which provides the creditor with special protection from liability provided the loan does not have certain features, such as negative amortization or balloon payment; the fees are within specified limits; and the creditor underwrites the mortgage payment using the maximum interest rate in the first five years. Third, a creditor operating predominantly in rural or underserved areas can make a qualified mortgage with a balloon payment. This option is meant to preserve access to credit for consumers located in rural or underserved areas where banks originate balloon loans to hedge against interest rate risk for loans held in portfolio. Finally, a creditor can refinance a "non-standard mortgage" with risky features into a more stable "standard mortgage" with a lower monthly payment. This option is meant to preserve access to streamlined refinancing.

Because rulemaking authority for TILA will transfer to the Bureau on July 21, 2011, the Board will not finalize this proposal. Public comments are due on July 22, 2011. Comments received by the Board will be transferred to the Bureau, which will assume responsibility for developing final rules.

II. The Board's Efforts to Improve Mortgage Disclosures

The Board issued three regulatory proposed rules as part of its comprehensive review of mortgage disclosures under TILA. The first phase of the review consisted of two proposals issued in August 2009, which would reform the consumer disclosures under TILA for closed-end mortgage loans and HELOCs. A third proposal, issued in September 2010, proposed changes to the disclosures for reverse mortgages, new disclosures for loan modifications, restrictions on certain advertising practices and sales practices for reverse mortgages, and changes to the disclosure obligations of loan servicers. The third proposal also included changes to the disclosures consumers receive explaining their right to rescind certain loans and would have clarified the responsibilities of the creditor if a consumer exercises this rescission right. In response to the three proposals, the Board received more than 5,000 comments expressing divergent views on many substantive and technical issues.

A. Closed-end Mortgage Disclosures

To shop for and understand the cost of credit, consumers must be able to identify and understand the key terms of the mortgage. In formulating proposed revisions to Regulation Z, which implements TILA, the Board used the results of consumer testing to ensure that the most essential information is provided at a suitable time using content and formats that are clear and conspicuous. With this in mind, in August 2009, the Board proposed to revise the disclosures for closed-end mortgage loans to highlight potentially risky features such as adjustable rates, prepayment penalties, and negative amortization. The disclosure would also show consumers how much their monthly payment might increase for an adjustable rate loan.

The Board also proposed to improve the disclosure of the APR so it captures most of the fees and settlement costs paid by consumers. As proposed, lenders would be required to include in the disclosure a graph that illustrates how the consumer's APR compares to the average rate offered to borrowers with excellent credit. The Board also proposed to require lenders to provide final TILA disclosures so that consumers receive them in all cases at least three business days before loan closing, even if there have been no changes from the early estimate provided at application.

B. HELOC Disclosures

The Board also proposed in August 2009 an entirely new disclosure regime for HELOCs. The proposal addressed the timing, content, and format of the disclosures creditors provide throughout the life of these open-end credit plans. In addition, the HELOC proposal would strengthen protections for consumers who have their home equity lines suspended or reduced in a declining market.

Currently, consumers receive lengthy, generic disclosures at application. Under the proposal, consumers would receive at application a new one-page summary containing basic information about HELOCs and the associated risks. Shortly after application, consumers would receive a disclosure that reflects the specific terms of their credit plans. At account opening, lenders would provide final disclosures in the same format to facilitate comparison with the earlier disclosures. Throughout the life of the plan, lenders would provide enhanced periodic statements, showing the total amount of interest and fees charged for the statement period and the year to date.

In addition, the proposal would prohibit creditors from terminating an account for payment-related reasons unless the consumer is more than 30 days late in making a payment. The Board further proposed to strengthen the consumer protections that apply when a consumer's credit line has been suspended or reduced, such as when property value has declined. Creditors would have to provide additional information about the reasons for the action and about the consumers' right to request reinstatement of the credit line. The rules also would require lenders to promptly investigate and respond to consumers' requests to have their credit lines reinstated.

C. Reverse Mortgages

In September 2010, the Board proposed significant changes to enhance consumer protections for reverse mortgage transactions. Under the proposal, the timing, content, and format of reverse mortgage disclosures would be changed to make the disclosures more useful to consumers. Currently, consumers typically receive lengthy disclosures at the time they apply that do not explain the particular features unique to reverse mortgages. As proposed, however, consumers would receive disclosures on or with the application form, using simple language to highlight the basic features and risks of reverse mortgages. Shortly after filling out the application, consumers would receive transaction-specific disclosures that reflect the actual terms of the reverse mortgage being offered.

In developing the proposal, the Board recognized that disclosures alone may not always be sufficient to protect consumers from unfair practices related to reverse mortgages. Reverse mortgages are complex products available to older consumers, some of whom may be more vulnerable to abusive practices. Concerns existed that some consumers, in order to obtain a reverse mortgage, have been forced to buy financial products that can be costly or may not be beneficial, such as annuities or long-term care insurance. Consequently, the proposal would address these concerns by prohibiting creditors from conditioning a reverse mortgage on the consumer's purchase of another financial or insurance product. Consumers would also be required to receive counseling about reverse mortgages before a creditor could impose nonrefundable fees or close the loan.

D. Impact of the Dodd-Frank Act

On February 1, 2011, the Board announced that it did not expect to finalize the three pending mortgage disclosure rulemakings under TILA prior to the transfer of authority for such rulemakings to the Bureau. Under the Dodd-Frank Act, general rulemaking authority for TILA is scheduled to transfer to the Bureau on July 21, 2011. The Dodd-Frank Act also requires that the Bureau issue a proposal within 18 months after the designated transfer date to combine, in a single form, the mortgage disclosures required by TILA and the disclosures required by RESPA. In light of that mandate and the upcoming transfer date, the Board carefully evaluated whether there would be public benefit in proceeding with the disclosure rulemakings initiated with the Board's August 2009 and September 2010 proposals. Because the Board's 2009 and 2010 TILA proposals would substantially revise the disclosures for mortgage transactions, any new disclosures adopted by the Board would be subject to the Bureau's further revision in carrying out its mandate to combine the TILA and RESPA disclosures. In addition, a combined

TILA-RESPA disclosure rule could well be proposed by the Bureau before any new disclosure requirements issued by the Board could be fully implemented by creditors.

For these reasons, the Board determined that proceeding with the 2009 and 2010 proposals would not be in the public interest. Although there are specific provisions of these Board proposals that would not be affected by the Bureau's development of joint TILA-RESPA disclosures, adopting those portions of the Board's proposals in a piecemeal fashion would be of limited benefit, and the issuance of multiple rules with different implementation periods would create compliance difficulties. Accordingly, the Board did not finalize the August 2009 and September 2010 proposals, which will be transferred and become proposals of the Bureau.

Conclusion

The Federal Reserve remains committed to carrying out its responsibilities for consumer protection, which will remain a priority for the Board notwithstanding the upcoming transfer of various rule-writing authorities to the Bureau. The Federal Reserve will retain a significant role in supervising financial institutions for compliance with both consumer protection regulations and the Community Reinvestment Act.

During the mortgage crisis of the past few years, we have witnessed the importance of effective consumer protection in preserving not only the well-being of particular communities, but more importantly, of the economy as a whole. The effectiveness of consumer regulations depends critically on strong supervision and enforcement, and the Federal Reserve will continue to take seriously its responsibility in these areas.

Summary of Federal Reserve Board Mortgage Rulemakings – 2008 through 2011

Final Rules

Rule	Date of Issuance	Description
Home Ownership and Equity Protection Act (HOEPA): Final Rule	July 2008 73 FR 44522 (July 30, 2008)	Rules to prohibit certain unfair or deceptive practices. For "higher-priced mortgage loans," the rules require creditors to assess a borrower's repayment ability and establish an escrow account. They also restrict the use of prepayment penalties. For all loans secured by a consumer's principal dwelling, the rules prohibit unfair servicing practices and the coercion of appraisers; include provisions to prevent misleading and deceptive mortgage advertising; and require transaction-specific disclosures within three days after application to aid mortgage shopping.
Mortgage Disclosure Improvement Act, Part I: Final Rule	May 2009 74 FR 23289 (May 19, 2009)	Rules to revise timing requirements for providing early disclosures in closed-end mortgage transactions.
Mortgage Disclosure Improvement Act, Part II: Interim Final Rule	September 2010 75 FR 58470 (Sept. 24, 2010)	Interim final rule to require creditors to disclose in a tabular format how a borrower's regular mortgage payment can change over time, along with a statement that the ability to refinance is not guaranteed.
Helping Families Save Their Homes Act – Mortgage Transfer Disclosure: Final Rule	September 2010 75 FR 58489 (Sept. 24, 2010)	Rule to require that consumers receive notice of the sale or transfer of their mortgage loan.
Loan Originator Compensation: Final Rule	September 2010 75 FR 58509 (Sept. 24, 2010)	Rules to prohibit unfair practices related to loan originator compensation, including a prohibition on paying compensation to an originator based on the interest rate or other loan terms (except the loan amount).
Dodd-Frank Act – Appraisal Independence: Interim Final Rule	October 2010 75 FR 66554 (Oct. 28, 2010)	Rules to ensure that appraisers are free to use their independent professional judgment in assigning home values. The rules also require that fee appraisers receive customary and reasonable payments for their services.
Dodd-Frank Act – Escrow Account: Final Rule	March 2011 76 FR 11319 (March 2, 2011)	Rule to provide a higher rate threshold for determining when escrow accounts are mandatory for jumbo loans.

Summary of Federal Reserve Board Mortgage Rulemakings – 2008 through 2011

Proposed Rules (not finalized)

Rule	Date of Issuance	Description
Regulatory Review of Disclosure Rules for Closed-end Mortgages (Phase I)	August 2009 74 FR 43232 (Aug. 26, 2009)	Proposal to revise disclosures for closed-end mortgage loans to highlight potentially risky features; improve the annual percentage rate (APR) disclosure so it captures most fees and settlement costs paid by consumers; and require final TILA disclosures at least three business days before loan closing, even if early estimates provided at application did not change.
Regulatory Review of Disclosure Rules for Home Equity Lines of Credit (HELOCs) (Phase I)	August 2009 74 FR 43428 (Aug. 26, 2009)	Proposal to revise the timing, content, and format of required disclosures for home equity lines of credit and strengthen protections for consumers who have their home equity lines suspended or reduced.
Regulatory Review of Mortgage Disclosure Rules (Phase II)	September 2010 75 FR 58539 (Sept. 24, 2010)	Proposal to revise reverse mortgage disclosures and protect consumers against unfair practices in reverse mortgage transactions; strengthen disclosure requirements for loan modifications; improve notices of a consumer's right to rescind a home mortgage; and prohibit deceptive and misleading advertising for home equity lines of credit.
Dodd-Frank Act – Escrow Account Disclosures	March 2011 76 FR 11598 (March 2, 2011)	Proposal to expand the minimum period for mandatory escrow accounts for first-lien, higher-priced loans and provide an exemption for certain creditors in "rural or underserved" counties. The rules would also implement new disclosure requirements for escrow accounts, both when escrow accounts are mandatory (*i.e.*, for "higher-priced mortgage loans") and when they are not.
Dodd-Frank Act – Ability to Repay/Qualified Mortgages	May 2011 76 FR 27390 (May 11, 2011)	Proposal to require that creditors determine a consumer's ability to repay a mortgage before making the loan and establish minimum mortgage underwriting standards. The proposal provides four options for complying with the ability-to-repay requirement, including making a "qualified mortgage" that does not have certain loan terms or features.

NATIONAL ASSOCIATION of REALTORS®
REALTOR®

500 New Jersey Avenue, N.W.
Washington, DC 20001-2020
202.383.1194 Fax 202.383.7580
www.realtors.org/governmentaffairs

TESTIMONY OF

STEVE A. BROWN
EXECUTIVE VICE PRESIDENT, CRYE-LEIKE REALTORS®

ON BEHALF OF

THE NATIONAL ASSOCIATION OF REALTORS®

BEFORE

THE UNITED STATES HOUSE OF REPRESENTATIVES COMMITTEE ON FINANCIAL SERVICES SUBCOMMITTEE ON INSURANCE, HOUSING, AND COMMUNITY OPPORTUNITY

HEARING REGARDING

MORTGAGE ORIGINATION: THE IMPACT OF RECENT CHANGES ON HOMEOWNERS AND BUSINESSES

JULY 13, 2011

INTRODUCTION

Madam Chairwoman, Ranking Member Gutierrez, and members of the Subcommittee, I am Steve Brown, Executive Vice President for Crye-Leike REALTORS®, based in Memphis, Tennessee. I thank you for the opportunity to participate in this hearing on behalf of the 1.1 million members of the National Association of REALTORS® (NAR). NAR represents a wide variety of housing industry professionals committed to the development and preservation of the nation's housing stock and making it available to the widest range of potential homebuyers.

Crye-Leike is a full service real estate company founded in Memphis in 1977. Today we are the nation's 6th largest real estate brokerage company and the largest serving markets in Tennessee, Arkansas, Georgia, Mississippi, and across the Mid-South. Crye-Leike has a network of more than 3600 licensed sales associates, 600 staff members and over 130 branch and franchise offices located in 65 counties throughout an eight-state region in Alabama, Arkansas, Florida, Georgia, Kentucky, Mississippi, Oklahoma, and Tennessee.

In my testimony today, I would like to cover a number of issues affecting the real estate and housing finance industry's ability to facilitate home sales and the mortgage origination process. These issues include the ramifications of the U.S. Department of Housing and Urban Development (HUD) 2010 guidance concerning the sale of home warranty contracts, issues arising as a result of the Qualified Mortgage (QM) provisions of the Dodd-Frank Wall Street Reform and Consumer Financial Protect law, the FHA mortgage program, appraisal oversight and proposed changes to the Real Estate Services Procedures Act (RESPA) and Truth in Lending (TILA) Act disclosures. But before I begin, I would like to thank the Chair and the Financial Services Committee for all of their hard work on extending the National Flood Insurance Program. As you know, the flood insurance program is vital to home owners and the housing industry in general and is particularly important where we do business and across the nation.

HOME WARRANTY

One major issue facing real estate firms, home warranty companies, and consumers is the treatment of home warranty under the Real Estate Settlement Procedures Act or RESPA. RESPA was enacted in 1974 to prevent kickbacks for referrals among settlement service providers for settlement services. A settlement service is customarily a service required to close the mortgage or settle a real estate transaction. The traditional settlement service providers are lenders, real estate agents and brokers, title agents and companies, appraisers, and attorneys. A home warranty is an insurance product that covers future repairs for a specified set of appliances or home systems and a period of time spelled out in the warranty contract. NAR has never believed home warranties are, in fact, a settlement service, and therefore subject to RESPA. Rather, we believe that this is an issue rightly regulated under state law as they currently are.

Despite the fact that a home warranty is clearly not a requirement for the origination of a mortgage or the sale of a home, the U.S. Department of Housing and Urban Development (HUD) nonetheless included home warranties in a list of settlement services in the RESPA regulation decades ago. The author of those regulations actually once told industry members that there was really no reason to include home warranty but since home warranties are often paid for at closing and that payment is reflected on the closing statement, home warranties were deemed a settlement service.

For nearly twenty years, this situation was not a problem until HUD issued a letter to a private citizen in 2008 that suggested the sale of home warranties by individual real estate agents was essentially a per se violation of RESPA. This arrangement has long been the business model of half the warranty industry. Their sales force are real estate agents and brokers who make the product known to their clients, explaining its features, processing the paperwork, and a number of other things, receive a small stipend for each completed transaction. This method of compensation is appropriate under RESPA's long-standing exception to its kickback provisions that allow a person to be paid for services actually performed. But the 2008 HUD letter made a significant change that has resulted in numerous class action lawsuits across the country.

NAR and its industry partners have spent over two years working with HUD to try to convince them the 2008 letter was harmful and incorrect. Home warranties are not a settlement service. They are not required by lenders to complete the transaction as settlement services are. They are purely optional. Many times, they aren't even purchased by buyers; sellers often offer them as a way to make the buyer feel more comfortable about the transaction. The fact that they typically are paid for at closing is simply due to the fact that most people want the coverage to take effect when they take possession of the property. That is just the right time to do it.

After years of working with HUD, the agency finally issued guidance in 2010. Unfortunately, that guidance is even more harmful than the original HUD letter. It is wholly unrealistic and ignores the actual services agents and brokers provide. Worse, it has led to even more class action lawsuits that are crippling real estate brokers and home warranty companies that are already strained by the current real estate market conditions. The lawsuits are likely to hurt consumers as well who won't have easy access to the product or will have to pay more for what is now a very reasonably priced product because warranty companies will have to hire a sales force and pay considerably more for the sales services currently provided by agents and brokers.

For these reasons, NAR and its industry partners are looking to Congress to correct this problem. We urge the subcommittee to pass H.R. 2446, the RESPA Home Warranty Clarification Act of 2011, introduced by Representatives Judy Biggert (R-IL) and Lacy Clay (D-MO), to countermand the HUD guidance and remove home warranties from RESPA and provide for appropriate consumer disclosure. Home warranties are already regulated at the state level; there is no need for another level of bureaucracy. HUD should never have included it all those years ago and the time is right to remove it now. Doing so will help save jobs and prevent consumers from having to pay more for a product they like.

DODD-FRANK 3% CAP ON AFFILIATES

Another area of concern to the industry is the definition of points and fees in the Qualified Mortgage (QM) provision of the Dodd-Frank Wall Street Reform and Consumer Protection Act. The definition is complicated but the effect is that mortgage companies with affiliates in the transaction such as a title company, must also count those charges towards a 3% cap on fees and points required by the bill's predatory lending safe harbor. A mortgage company without affiliates does not have to do so. So in many cases, affiliated companies would not be able to offer full service to clients because in doing so they would violate the 3% cap.

This is unfair for a number of reasons. First, the likelihood that the affiliate title company would charge an uncompetitive rate is slim. The title industry and title insurance rates are heavily regulated by the states. So the rates charged by affiliated and unaffiliated firms are will vary little. Second, a lender cannot "mark-up" affiliate charges because to do so would violate RESPA. Third, surveys show that consumers say they save money by using the affiliates and it makes transactions easier.

The House addressed this issue in its version of Dodd-Frank through an amendment by Representative Clay of Missouri. However, for some unknown reason, it was removed during the conference. To this day, no explanation has been given for its removal other than it might have been a mistake. Congress should fix the 3% cap issue at its earliest opportunity so consumers can fully benefit from greater competition in the lending industry between affiliated and unaffiliated lenders.

FHA

I would also like to take time to reiterate the importance of the FHA program and making permanent the existing FHA and GSE loan limit formula. With credit already tight, FHA is playing a vital role in providing affordable, well-underwritten mortgage credit to American families. This is a role that FHA has long played without costing taxpayers a penny. In fact, FHA throughout its history has routinely returned funds to the Treasury.

Loan limits

Changing the FHA and GSE loan limit formulas will result in significant declines in the current loan limits. In fact, we have already heard that one of the nation's largest lenders has already dropped their loan limits effective July 1, 2011 in anticipation of the expiration of current loan limits on September 30, 2011. This will hurt the housing recovery by reducing access to safe affordable FHA loans in 669 counties in 42 states plus the District of Columbia; only eight states would not be impacted.[1] The resulting average reduction in limits will be more $68,000. With this decline, 27 percent of all owner-occupied homes in the United States will be ineligible for GSE financing, and more than 59 percent of all owner-occupied housing will be ineligible for FHA financing.[2] In states where we operate, FHA is used by more than 60 percent of our buyers. These declines will have a dramatic impact on liquidity in our markets, and could halt the housing recovery.

Reducing the loan limits could also result in a greater risk to the stability of the FHA program since higher balance FHA loans perform better than lower balance ones. According to the FY 2009 FHA Mutual Mortgage Insurance Fund (MMIF) audit, "FHA experience indicates that larger houses tend to perform better compared with smaller houses in the same geographical

1. Arkansas, Iowa, Kansas, Mississippi, Nebraska, Oklahoma, North Dakota, and South Dakota.
2. According to data compiled by the National Association of Home Builders, "GSE and FHA Loan Limit Changes for 2011: Scope of Impact"

area, all else being equal."[3] So despite arguments that FHA higher limits put taxpayers at risk, these loans actually add strength to the program and reduce risk to the Fund.

Many critics calling for a rollback of loan limits have justified their position by arguing that the FHA loan program was always intended to only benefit low-income or first time borrowers. However, this is a misconception. If you take a look back at the program's history, you will find that this is not the case. A review of the program's earliest loan limits indicates that the FHA loan limit in 1930 was $16,000. The national median home value in 1930 was $4,778.[4] The majority of homes were valued between $2,000 and $7,500, with the largest number of them falling between $3,000 and $5,000.[5] Only 3.2 percent of homes were valued between $15,000 and $20,000.[6] So the upper limit of $16,000 was more than 330 percent of the median American home value at that time. Contrast that with today, where even the current higher loan limits are set at 125 percent of the local area median home price. Even at its inception, FHA was intended to provide safe, affordable mortgage financing for all homebuyers in all markets – high and low cost.

With housing markets struggling to recover, the last thing we need to do is to put an avoidable stumbling block in the path of a much needed housing recovery. I know that it has been said before, but I believe it bears repeating – without a housing recovery, the nation's economy as a whole will struggle to recover its balance. This is not the time to be scaling back mortgage loan limits.

For these reasons, I and my fellow REALTORS® strongly urge this Subcommittee to approve H.R. 1754, the "Preserving Equal Access to Mortgage Finance Programs Act." This bill, introduced by Representatives Gary Miller (R-CA) and Brad Sherman (D-CA) will make the current limits for FHA and the GSEs permanent and ensure that families across the country have ongoing access to safe, affordable mortgages.

Downpayment Requirements

We also believe the downpayment for FHA should remain at 3.5% and that other requirements should also remain at current levels. FHA's book of new business (written since 2009) is performing extremely well and there is no reason to make more restrictive changes in the name of creating a false sense of "cleaning up" the real estate financing problems of the past. In fact, the current stagnant market could be sent in to a deeper, more serious downward spiral with any increase in the downpayment requirement.

In the case of downpayments, proposals to further increase FHA downpayment requirements are not only unwarranted but will not serve the purposes that proponents seek. First of all, increasing FHA's downpayment will not add a penny to FHA's reserves. The reserves can only

3. *Actuarial Review of the Federal Housing Administration Mutual Mortgage Insurance Fund (Excluding HECMs) for Fiscal Year 2009*, by Integrated Financial Engineering Inc., November 6, 2009, pg. 45.
4. Id. at 18
5. Id.
6. 15th Census of the United States, Population, Volume VI: Families, U.S. Census Bureau, 1930, P. 17

be increased by collecting premiums, and rising home prices. Increasing downpayments does not put any additional money into reserves; it simply reduces the amount of the mortgage.

Second, while a higher downpayment requirement would increase an individual borrower's investment in a home, such an increase will disenfranchise many of the borrowers that the FHA has successfully served throughout its history. According to our estimates based on very conservative assumptions, it would take the average American family, acting frugally, nearly 7 years to save for a 5 percent downpayment and the closing costs that average 3-5 percent of the purchase price on a $200,000 home, and more than 10 years to save 10 percent down. A 20 percent downpayment on the same home would require 17.3 years of saving for this same family. Given the very conservative assumptions inherent in our calculations, it is apparent that increasing downpayment requirements will create a substantial burden for all American homebuyers and especially younger families.

This increased burden comes with only marginal benefits. Research has shown that requiring a higher downpayment does little to reduce risk of default, but can strip homebuyers of their savings and increases the number of borrowers who would be ineligible for homeownership.

A recent study demonstrated that:

- Increasing a downpayment requirement from 5 percent to 10 percent reduces default rates by only 2/10ths of one percent, but could disenfranchise more than 8 percent of homebuyers.
- Increasing the downpayment requirement from 5 percent to 20 percent would reduce default rates by only 6/10ths of one percent, but would disenfranchise over 20 percent of homebuyers.[7]
- For FHA, increasing the downpayment requirement from 3.5 percent to 5 percent would disenfranchise more than 300,000 responsible homebuyers.[8]

If there is one lesson to be learned from the recent housing crisis, it is that the key to minimizing foreclosures and defaults is sound and careful underwriting and NOT downpayments.

Condominiums

HUD could further help the housing recovery by leveling the playing field for condominium loans. FHA recently unveiled new condominium rules in an effort to clarify, expand, consolidate and update existing guidance. The new guidance provides increased flexibility for FHA to address individual circumstances so that the agency can be more effective at the neighborhood level. While we applaud their efforts, we recommend further changes to FHA's condominium rules that will provide greater liquidity to this sector of the real estate market

7. Study done by the Community Mortgage Banking Project, "Study of 33 Million Home Loans Shows that Quality Underwriting Standards Reduce Default More than mandatory Down Payments."
8. HUD Testimony, before the House Financial Services Subcommittee on Housing and Community Opportunity, March 11, 2010

without causing additional risk to the MMIF. We support enhancements made to the rules but believe more needs to – and can - be done.

After taking numerous steps to mitigate risk, FHA's purchase activity is performing as well as it has in any period since Neighborhood Watch was established in 1999. For the quarter ending on March 31, 2011, the Seriously Delinquent and Claims Rate was 2.26 percent, which is the lowest rate for any quarter over the last two years. Condominium loans are performing even more strongly than other purchase loans. According to the most recent data, condominium purchases had a delinquent/claims rate of 1.01 percent for existing condominium projects and 1.28 percent for new projects, both of which are less than half of the overall claims rate.

Further amending the rules for condominium developments will benefit all parties in the real estate transaction. Lenders will have the opportunity to move more REO properties off their books because more units could be eligible for buyers with FHA mortgages. Individuals and families purchasing units in these developments with FHA loans will have access to more flexible and affordable financing opportunities. Potential buyers with FHA mortgages will have a wider choice of condominium developments. Existing owners in these developments benefit as vacant units are purchased and occupied and the owner-occupied ratio increases. Improving the health of condominium developments will reduce risk to the insurance fund. Considering the strong performance of recent loans made under the revised underwriting criteria makes a compelling case that more relaxed rules would be beneficial.

APPRAISALS

REALTORS® support and encourage credible, independent appraisals and valuations of real property, which are critical to the health of the overall real estate industry. A trustworthy valuation of real property 1) ensures the real property value is sufficient to collateralize the mortgage, 2) protects the homebuyer, 3) allows secondary markets to have confidence in the mortgage products and mortgage backed securities, and 4) builds public trust in the real estate profession. Professionally developed valuations provide an independent, objective analysis of real property. Valuations that are not credible or not independent harm communities and result in unintended consequences. The purchase of a home is the largest investment most people make. A valuation that does not properly reflect the owner's equity and may require the owner to pay increased fees or inject unneeded additional liquidity into a collateralized loan to meet higher lending requirements. Valuations of real property that are too high give a false sense of security to homeowners seeking access to the equity in their homes and to lenders making a determination as to the security of their loan. Valuations that are too low may create a downward cycle of economic deterioration for neighborhoods and communities and cause increased cash requirements on lenders.

NAR supports the appraisal provisions of the Dodd-Frank Wall Street Reform and Consumer Protection Act, including language that enhanced federal oversight of state appraisal programs. The Appraisal Subcommittee is primarily responsible for this oversight and in fiscal year 2010 conducted 34 on-site visits of which, 26 were full Compliance Reviews. The oversight work will increase for ASC in the coming years as states implement legislation and rules on the registration of appraisal management companies (AMCs).

One of the biggest challenges to federal oversight of state appraisal programs is the current funding structure of appraisal programs at the state level. Typically, licensing and certification fees paid by the appraisers to the state are to be used for funding state appraisal boards. However, in many cases these fees are directed to a state's general fund, causing the state appraisal board to compete with other state discretionary programs for funding. Inadequate funding of state appraisal boards means that recommendations offered by ASC through site visits and Compliance Reviews are difficult, if not impossible, to implement.

RESPA/TILA DISCLOSURES

NAR is participating in the effort by the Consumer Financial Protection Bureau (CFPB) to combine the Truth in Lending Act (TILA) Disclosure with the RESPA Good Faith Estimate (GFE). NAR has been a strong supporter of reducing duplicative paperwork and combining these two forms provided the combined document includes the statutorily required elements of both laws. To date, NAR has been pleased with the manner in which the CFPB is handling its task. It has been open and sought input regularly as it combines and makes adjustments to its proposed forms. Any concerns we have expressed have been addressed in subsequent drafts. We have found the process so far to be superior to many previous regulatory experiences with other agencies.

Our only concern over the long term is that when new forms are implemented, every effort must be made to reduce the costs of transition and that there is adequate educational effort made to explain the new forms, how they work and how they are properly completed and used.

CONCLUSION

These five issues are but a few of the headwinds facing the housing industry. NAR opposed risky lending in 2004 when it issued its subprime lending policy that called for strong underwriting on mortgages and measuring a person's ability to repay. We feel now that the pendulum has swung too far and with new regulations on the horizon, fewer and fewer otherwise qualified people will be able to get a loan and there will be fewer lenders to lend. Congress and the Administration need to seriously re-examine the many well-meaning laws and regulations that have come out of the financial and mortgage crisis. Some have merit and need minor fixes; others may have sounded good at the time but are proving problematic at best. They deserve a second look to ensure the still fragile recovery stays on track and protect the long-term value of homeownership in the U.S.

NAR thanks the Subcommittee members for their attention to these vital issues. We look forward to working with Congress on efforts to address the challenges still facing the nation's housing markets.

Testimony of Kelly Thompson Cochran
Deputy Assistant Director, Office of Regulations
Consumer Financial Protection Bureau
Before the Subcommittee on Insurance, Housing and Community Opportunity
Committee on Financial Services
United States House of Representatives
Wednesday, July 13, 2011

Introduction

Thank you, Chairman Biggert, Ranking Member Gutierrez, and members of the Subcommittee for inviting me to testify about the work of the Consumer Financial Protection Bureau ("CFPB" or "Bureau"). On behalf of the CFPB, I appreciate the opportunity to testify about the CFPB's work in simplifying mortgage loan disclosures.

Last year, the Dodd-Frank Wall Street Reform and Consumer Protection Act (the "Dodd-Frank Act") not only created the CFPB, but also amended Federal statutes governing mortgage loans, including the Truth in Lending Act ("TILA") and the Real Estate Settlement Procedures Act ("RESPA"). The amendments require the CFPB to publish a single, integrated model disclosure for mortgage loan transactions that includes disclosure requirements of both TILA and RESPA.[1] The purpose of the integrated disclosure is to "facilitate compliance" with TILA and RESPA, and to aid borrower understanding of the transaction "by utilizing readily understandable language to simplify the technical nature of the disclosures."[2] The Dodd-Frank Act requires the CFPB to publish proposed new forms and regulations by July 21, 2012. It is worth noting that the integration of these disclosures is not a new idea. It has been the subject of legislative and regulatory actions since 1996.[3]

To satisfy this important statutory mandate, the CFPB has made the integrated TILA/RESPA disclosure project one of its very highest priorities. To inform our efforts at the outset, the CFPB has conducted extensive public outreach, including to consumer and industry groups, to obtain comments and feedback on issues concerning the current disclosures. In May, I was pleased to participate in a CFPB bipartisan briefing for Committee staff and to get their comments and suggestions, and very much appreciate the opportunity today to testify before the Subcommittee on our progress on this important undertaking. We are pleased to report that consumers and industry alike have reacted positively to the draft forms and the development process being used by the CFPB.

Integration and Simplification

The Act states that one of the purposes of the integrated disclosure is to aid consumer understanding by using readily understandable language. At the CFPB, we believe that a simple

[1] Dodd-Frank Act, §§ 1032(f), 1098, 1100A. This requirement is codified in RESPA and TILA at 12 U.S.C. § 2603(a) and 15 U.S.C. § 1604(b), respectively.
[2] *Id.*
[3] *See* Economic Growth and Regulatory Paperwork Reduction Act of 1996, P.L. 104-208, Tit. II, § 2101.

and straightforward presentation of key credit terms is the best way to achieve this purpose. Our goal is shorter, clearer forms—the kind that consumers can read in a few minutes with high levels of understanding. We have focused on making it easier for consumers both to understand the key terms of the loan they have been offered and to compare offers to find the loan that best meets their needs.

The Act sets forth a second purpose of the integrated disclosure, which is to facilitate compliance with TILA and RESPA. We understand the deep frustration from lenders, brokers, and other market participants across the country_that the current forms are complicated, duplicative, and expensive to fill out. We are striving to make the disclosure easier for industry to complete and use. We are also working to address implementation burdens as we move through the design process by gathering broad feedback from lenders, document service providers, other real estate settlement service providers, and other technology companies that serve the mortgage lending industry.

In short, the CFPB is working to give consumers the transparency they need to choose the mortgages that work best for themselves and their families, while at the same time eliminating unnecessary regulatory burdens for lenders.

Our Work

The disclosure integration project has been a high priority since the beginning of our efforts to stand up the Bureau. We began our work on the disclosure last fall when we sponsored a roundtable at the Treasury Department that brought together lenders and consumer advocates to discuss how to simplify federal mortgage loan disclosures. Consumer groups explained that many consumers did not use disclosures to assess costs or to compare alternatives because the current forms are complicated and hard to use. The current disclosures came under even more intense criticism from those who have to explain them to consumers and those who have liability for errors. Mortgage originators described the forms as costly to complete and typically confusing and unhelpful to their customers. Many originators have developed additional documentation to try to clear up confusion, which of course results in even more paperwork.

Over the next eight months, we reviewed research, conducted additional outreach, and began the process of analysis and design. This process included meetings with all sectors of the industry, from large financial institutions to small settlement service providers, to obtain information about the issues the industry faces in connection with these disclosures. In addition, we met with consumer advocacy groups and spoke with housing counselors to discuss the consumer experience with the disclosures. We met with other regulatory agencies to learn about their experiences and gain their perspectives. We also held an academic symposium to gather the latest information about research on consumer understanding of complex financial information.

On May 18, 2011, we released two prototypes of integrated disclosures for provision to consumers within three days of application. Both prototypes were two pages long, with different first pages and virtually identical second pages. We tested these two drafts through one-on-one interviews with consumers, lenders, and brokers in Baltimore, Maryland. Based on the results of this testing, and additional public feedback described below, we revised the draft disclosures.

On June 27, 2011, we released a second round of prototypes, both of which had the same first page, but featured two different methods of presenting estimated settlement costs and related information on the second page. Two weeks ago, we tested this second round of draft disclosures in Los Angeles, California, and gathered additional public feedback. We expect to conduct several additional rounds of revision and testing into the fall, with testing sites in Springfield, Massachusetts; Albuquerque, New Mexico; Chicago; and Birmingham, Alabama.

Know Before You Owe

At the same time that we started the testing described above, we also launched an Internet-based effort to solicit broad-based input in the development of the new TILA/RESPA forms.[4] This initiative, which we are calling "Know Before You Owe," is designed to obtain feedback throughout the development process from a range of consumers, advocates, housing counselors, industry stakeholders, and anyone else with an interest in these issues from across the country. We are taking in this broad feedback well in advance of the formal process of notice-and-comment for official rulemaking.

The Know Before You Owe project features an interactive tool on the CFPB's website to gather public feedback about the designs. There are slightly different versions to seek consumer and industry input, with additional questions on the industry input tool to focus on implementation issues. Each round of formal testing of the draft disclosures coincides with a round of public feedback through the Know Before You Owe initiative. We are sharing the input we receive from Know Before You Owe with our testing team and designers, and factoring it into our design process as we refine our prototypes.

We have been extremely pleased with the significant public response to this initiative. In response to our posting of the two initial prototypes, more than 13,000 users provided written feedback. More than 7,000 came through the consumer version of the Internet tool and more than 5,000 through the industry version. Input came from all over the country, including cities such as Plano, Texas; Columbia, South Carolina; Billings, Montana; Overland Park, Kansas; and Minneapolis. The second round of the project was launched in late June and drew written feedback from almost 4,000 users.

To our knowledge, we are the first federal financial services agency to seek such broad-based public input this early in the design process—in advance of proposing a rule—for a consumer disclosure. This is a learning process for us and for the participants. The public feedback has generally been consistent with the testing results, and has provided valuable comments and suggestions. We believe this process can be particularly useful in identifying potential implementation issues that may arise for different kinds of financial services providers, and in helping us to address those issues before final design decisions are made.

Regulatory Perspective

---

[4] See http://www.consumerfinance.gov/knowbeforeyouowe/.

In the coming months, we will accelerate work on the regulations underlying the disclosure forms and on developing the integrated closing-stage disclosure. As contemplated by the Dodd-Frank Act, we also will review proposed mortgage-related rules under TILA that were issued but not finalized by the Board of Governors of the Federal Reserve System to the extent that the proposals address issues relating to the mortgage disclosure project. We also expect to convene a panel to consult with small businesses regarding potential impacts prior to proposing a rule, and to consult with the prudential regulators and other relevant agencies.

On July 21, 2011, the Bureau will assume responsibility for various rulemakings mandated by the Dodd-Frank Act under statutes that will transfer to the CFPB, including other rulemakings that relate to mortgage origination activities. We are currently studying the Act's amendments to these statutes, as well as existing regulatory provisions and proposals, to prepare for that transfer of authority. Under Title XIV of the Dodd-Frank Act, a number of these rulemakings must be completed by January 2013.

Conclusion

Chairman Biggert, Ranking Member Gutierrez, and members of the Subcommittee, thank you again for inviting me to testify today about the CFPB's integration and simplification of mortgage loan disclosures. We know that no one project can solve all issues regarding mortgage originations, but we remain convinced that simple, streamlined mortgage disclosures are a critical reform that can provide both more value for borrowers and reduced burdens for lenders. We welcome the opportunity to discuss our efforts and to update you on our progress.

MORTGAGE BANKERS ASSOCIATION
Investing in communities

Statement of Henry V. Cunningham Jr., CMB

on behalf of the
Mortgage Bankers Association

House Financial Services Committee
Subcommittee on Insurance, Housing & Community Opportunity

"Mortgage Origination: The Impact of Recent Changes on Homeowners and Businesses"

July 13, 2011

1717 Rhode Island Ave., NW | Washington, DC 20036 | www.mortgagebankers.org |
(202) 557-2700

Chairwoman Biggert, Ranking Member Gutierrez and members of the subcommittee, my name is Hank Cunningham and I am the president of Cunningham and Company, an independent mortgage banking firm with offices throughout North Carolina. I have more than 37 years of professional mortgage experience and currently serve as Chairman of the Residential Board of Governors of the Mortgage Bankers Association.[1] I also serve on MBA's Board of Directors.

My testimony will focus on the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (Dodd-Frank), and specifically the Credit Risk Retention proposed rule, and its Qualified Residential Mortgage (QRM) exemption, and the Ability to Repay proposed rule, and its Qualified Mortgage (QM) safe harbor, both of which are of enormous significance to our industry. I will also address the recent SAFE Mortgage Licensing Act and Loan Originator Compensation rules, which, although they are final, deserve refinements, as well as the Interim Appraisal Rule. Finally, I would like to address the RESPA/TILA effort where a rulemaking is anticipated in the fall.

I very much appreciate the opportunity to testify and plan to address these subjects and provide MBA's views.

Background

Less than a year ago, Congress passed Dodd-Frank. While it is too early to assess the full impact of this historic legislation, it is clear that the mortgage industry has been directing very considerable resources at implementing and responding to an avalanche of new and proposed regulations.

MBA recognizes that mortgage lenders need to take responsibility for their share of excesses during the recent housing boom. We recognize that changes are needed to ensure such excesses will not be repeated in the future. Indeed, we favor both reasonable risk retention and ability to repay requirements.

---

[1] The Mortgage Bankers Association (MBA) is the national association representing the real estate finance industry, an industry that employs more than 280,000 people in virtually every community in the country. Headquartered in Washington, D.C., the association works to ensure the continued strength of the nation's residential and commercial real estate markets; to expand homeownership and extend access to affordable housing to all Americans. MBA promotes fair and ethical lending practices and fosters professional excellence among real estate finance employees through a wide range of educational programs and a variety of publications. Its membership of over 2,200 companies includes all elements of real estate finance: mortgage companies, commercial banks, thrifts, Wall Street conduits, life insurance companies and others in the mortgage lending field. For additional information, visit MBA's Web site: www.mortgagebankers.org.

Nevertheless, the sheer quantity of rules is placing great stress on lenders, particularly smaller lenders who serve communities throughout the nation every day. Lenders are scaling back the number of production employees as business declines, but are offsetting those cuts with new compliance hires. This kind of trade off is both undesirable and unsustainable.

Most lenders know we will never be "too big to fail" but we also wonder if we are "too small to comply," raising the very real possibility that borrowers may lose our services and the important competition we bring to the market.

As we face this avalanche, we also know the market itself has largely cleared out toxic mortgage products, credit is tight and that rules already in place have limited the availability of mortgage credit to only highly qualified borrowers. The economy is sputtering and the housing market impedes recovery.

For all these reasons, we urge that federal regulators act judiciously with respect to regulations going forward. We need to make sure that efforts to provide a safe and sound housing market do not lead to an overreaction that risks making sustainable mortgage credit unnecessarily costly and unavailable to far too many families.

All of these rules, if finalized with the proper adjustments or revised, can help facilitate the provision of sustainable mortgage credit to the widest array of qualified borrowers at the most affordable costs. But, if they follow the wrong track, they risk lessening competition, increasing the cost of credit, and harming the very people they were designed to protect.

We respectfully urge Congress to carefully monitor all these new rules – those newly proposed and others recently finalized – to make certain they do not unwittingly harm American families, the mortgage market or the nation's economic recovery.

I. Risk Retention and Qualified Residential Mortgages

The ability to repay rule and the credit risk retention rule are the two most significant mortgage-related rules to come out of Dodd-Frank. Both of these rules have been proposed and comments are due on July 22 and August 1 respectively. Because they will affect the availability and affordability of mortgage credit for years to come, these rulemakings deserve the most careful attention of the regulators and Congress.

The risk retention rule, which contains the definition of Qualified Residential Mortgage, was proposed by six federal agencies. Under Dodd-Frank, asset-backed securities may not be issued without retention of a portion of credit risk by the securitizer unless the loan is a QRM. While estimates vary, the clear result of any risk retention rule will be that loans that are not QRMs will be costlier or not available at all.

Regrettably, the regulators have proposed a QRM definition that includes a high down payment[2] and uncommonly low loan-to-value (LTV)[3] and debt-to-income (DTI) ratios[4] that would make most loans subject to risk retention, and therefore costlier and in some cases unavailable. These effects will be worse for minority and moderate income borrowers who can least afford increased credit costs.

Like Congress, we do not believe risk retention is necessary where loans are determined to be QRM. Moreover, we believe the proposal for a narrow QRM is inconsistent with what Congress intended and would drastically limit affordable mortgage financing options to moderate income families, first-time borrowers, minorities, and many others.

The government's own data shows that the proposed regulations would hurt consumers by limiting access to credit for well-qualified borrowers.[5] Even high quality loans would not meet the proposed QRM requirements. Though 2009 was a year of highly conservative underwriting standards, only 30 percent of loans purchased by Fannie Mae and Freddie Mac would have met the proposed requirements. In effect, the QRM tightens credit in an already constricted lending environment.

Data also shows it could take moderate income borrowers, depending on where they live, up to 18 years to save for a 20 percent down payment for a moderately priced home.[6] The proposed "alternative" of ten percent down payment is not much better. It will take renters much longer to save. Borrowers also must pay closing costs, which typically add another $5,000 to the amount a borrower must save.

At the same time, borrowers who have faithfully made their mortgage payments but have little equity and may live in areas of significant home declines will find it difficult if not impossible to refinance into a QRM loan because of the proposal's 75 percent LTV requirement for refinancing.

---

[2]The proposed QRM would establish minimum down payment for purchase transaction of at least 20 percent of lesser of purchase price or property value plus closing costs.

[3] Specific maximum LTV requirements for QRM of not more than 80 percent for purchase loans, 75 percent CLTV for rate and term refinancings (includes first lien and any other closed end or open end credit on property) and 70 percent of CLTV for cash out refinances.

[4] Would establish maximum front-end and back-end DTI ratio of 28 and 36 to qualify.

[5] FHFA. Mortgage Market Note 11-02: Qualified Residential Mortgages. April 11, 2011

[6] MBA analysis of Census Bureau, Bureau of Labor Statistics, and National Association of Realtors data.

MBA's Position

MBA has made it a top priority, and is working in harmony with a very wide coalition of consumer advocates, civil rights groups and other industry associations, to educate policy makers and legislators concerning this rule. We have concluded that better mortgages for investors and homeowners alike could be accomplished if the final rule simply defined a QRM to exclude loans with risky product features and required documentation and verification as part of loan underwriting. While we support reasonable credit risk retention requirements, specific down payment, LTV and DTI requirements are unnecessary and not worth the societal costs of excluding far too many qualified borrowers from the most affordable mortgage loans to achieve homeownership.

We appreciate Congress's interest in this rule, which has led to a letter from more than 300 members asking that the proposal be reconsidered. We urge you to continue pressing to have this rule re-thought and redirected by regulators. We believe it should be changed to offer similar if not identical standards to the Qualified Mortgage, discussed below, and to repropose the rule along those lines. If that does not occur, we urge Congress to act as necessary to revise the law to assure that affordable credit is available to qualified families and private capital is invited back into the market as Congress intended.

II. Ability to Repay and Qualified Mortgages (QMs)

The proposed ability to repay and QM requirements under Title14 of Dodd-Frank share the same general purpose as the Credit Risk Retention and QRM requirements. Both provisions seek to ensure that mortgages are well underwritten and present a low risk of default.

To achieve this objective, Section 1411 of Dodd-Frank prohibits a creditor from making a mortgage loan unless the originator makes a reasonable determination, in good faith, based on verified and documented information at the time the loan is consummated, that the consumer has the ability to repay the loan, including all applicable taxes, insurance and assessments. Section 1412 also provides that if the loan meets the QM definition, it is presumed to meet the ability to repay requirements. The Board of Governors of the Federal Reserve System (Board) is charged with prescribing rules to implement Section 1412. Under Dodd-Frank, authority for TILA regulation and these provisions transfers to the Bureau of Consumer Financial Protection (CFPB) on July 21, 2011.

Dodd-Frank amended TILA to increase the penalties for violations, including violations of the ability to repay and anti-steering provisions. Section 1416 allows consumers who bring timely action against a creditor for a violation of the ability to repay requirements to recover special statutory damages equal to the sum of all finance charges and fees paid by the consumer unless the creditor demonstrates failure to comply is not material. Damages may be in addition to actual damages; statutory damages in individual or class actions, up to a prescribed threshold; and court costs and attorney fees. Violations can also provide a defense by recoupment and set off in a foreclosure action, without regard to any time limits on private actions.

The proposed rule implementing these provisions was issued by the Board on April 19, 2011, and published in the Federal Register on May 11, 2011. Consistent with the statute, the proposal would amend TILA regulations (Regulation Z)[7] to prohibit creditors from making a mortgage loan without regard to the consumer's ability to repay the loan. The proposal notes that the final rule will be issued by the CFPB.

The proposal would allow creditors to comply by originating a mortgage after considering and verifying eight factors[8] and basing the mortgage payment calculation on the fully indexed interest rate or originating a QM, which would provide decreased liability. The Board offered two alternative approaches to QM that come with different degrees of protection from liability.

Alternative 1 would operate as a "legal safe harbor" that the ability to repay requirement has been met and would define a QM as a mortgage that: (1) does not include negative amortization, interest-only payments, or balloon payments (except as permitted for balloon payment qualified mortgages) or has a loan term exceeding 30 years; (2) has total points and fees not exceeding three percent of the total loan amount ; and (3) where underwriting (a) is based on the maximum interest rate in the first five years, (b) uses a payment schedule that fully amortizes the loan over the loan term, and (c) takes into account any mortgage-related obligations. The income or assets of the borrower must also be considered and verified.

---

[7] 12 CFR 226

[8] These eight factors include: (1) consumer's current or reasonably expected income or assets, other than the value of dwelling that secures loan; (2) if creditor relies on income from consumer's employment in determining repayment ability, consumer's current employment status; (3) monthly payment on mortgage calculated based on fully indexed rate and monthly fully amortizing payments that are substantially equal; (4) consumer's monthly payment on any simultaneous loan creditor knows or has reason to know will be made including, HELOC payment using payment required under plan and amount of credit drawn at consummation of transaction; (5) consumer's monthly payment for mortgage-related obligations; (6) consumer's current debt obligations; (7) consumer's monthly debt-to-income ratio, or residual income; and (8) consumer's credit history.

Alternative 2 would establish a "rebuttable presumption of compliance" that the ability to repay requirement has been met for loans meeting the requirements listed in Alternative 1 and which also meets certain additional underwriting requirements including considering and verifying: (1) the consumer's employment status, (2) the monthly payment for any simultaneous mortgage, (3) the consumer's current debt obligations, (4) the monthly DTI ratio or residual income, and (5) the consumer's credit history.

Both alternatives provide that points and fees cannot exceed three percent of the loan amount. Points and fees would include: (1) compensation paid directly or indirectly by a consumer or creditor to a mortgage originator apparently including lenders and mortgage brokers as well as originator employees; (2) mortgage insurance premiums in excess of the amount payable under the Federal Housing Administration (FHA) program; and (3) the total prepayment penalty incurred by the consumer if the loan is refinanced by the existing holder of the loan. The proposal also provides exceptions to the calculation of points and fees for: (1) any bona fide and reasonable third-party charge not retained by the creditor, loan originator, or an affiliate of either, and (2) certain bona fide discount points.

As required by Dodd-Frank, the proposal would adjust the three percent limit for "smaller loans" that are defined as loans less than $75,000 on a sliding scale, or in the alternative, using a formula of up to five percent for loans under $20,000.

The rule also would: (1) provide an additional QM exception for a small creditor operating predominantly in a rural or underserved area originating a "Balloon Payment Qualified Mortgage"[9] and (2) establish an exception to the ability to repay requirement for Refinancing a "Non-standard Mortgage" into a "Standard Mortgage."[10]

MBA's Position

The ability to repay requirement will apply broadly to all mortgage loans and its violation will bring considerable liability not only to lenders but to assignees. MBA's view is that if

[9] Creditor and balloon mortgage must meet requirements in proposal including all requirements for qualified mortgage (except balloon payment allowed), including limits on points and fees; plus loan term of five years or more, and payment calculation based on scheduled periodic payments, excluding balloon payment. Creditor must be small and operating predominantly in rural or underserved area.

[10] Loans that are (1) adjustable-rate with an introductory fixed interest rate for a period of years, (2) an interest-only loan, and (3) a negative amortization loan can be refinanced into a "standard mortgage," not containing negative amortization, interest-only payments, or balloon payments; and which are subject to limits on points and fees may be refinanced without the creditor having to verify income or assets with written documentation, as long as the creditor for the existing mortgage and new mortgage are the same; borrower has a positive payment history on the existing mortgage; and payment on the new mortgage must be lower than the existing payment.

a QM definition is well structured, it will be the chosen means for lenders to comply and, therefore, the best way to incent the sound underwriting that Dodd-Frank seeks to ensure.

Safe Harbor

Having carefully considered the proposed alternatives, MBA strongly believes the QM test should be established as a safe harbor with bright lines to best ensure that the definition achieves its intended purposes. MBA's formal comments to the proposal will strongly urge that:

(1) The CFPB finalize a definition of QM as a bright line safe harbor to ensure safer, well documented, well underwritten mortgages, without unduly limiting the availability, or increasing the costs of, credit to borrowers; and including documentation and verification requirements as well as restrictions against riskier products;

(2) The limit on total points and fees in the QM alternatives proposed should be revised to provide (a) a more realistic definition of smaller loans; (b) exclusions for all third party fees regardless of affiliation with the lender; (c) exclusion of employee compensation to avoid double counting and (d) the exclusions otherwise provided in the proposal, such as certain up-front mortgage insurance premiums and up two discount points (depending on the reduction in rate); and

(3) QM safe harbor requirements be adopted as a basis for the QRM. A sound QM definition structured as a safe harbor should substitute for the QRM definition proposed. A sound safe harbor would incent sustainable mortgages that serve the interests of investors, as well as borrowers. Such a definition, covering all loans would invite private capital back into the market.

In MBA's view, a safe harbor would:

(1) Provide the strongest incentive for lenders to operate within its requirements and, at the same time, allow them to provide sustainable mortgage credit to the widest array of qualified borrowers;

(2) Still allow focused litigation, to determine whether the safe harbor requirements have been met, offering the most efficient and least costly means of resolving

claims; lenders who seek to best serve their borrowers and follow the rules should not be dogged by endless and costly litigation.

A presumption of compliance, on the other hand, would increase liability and borrower costs while lessening the availability of credit to some borrowers and increasing risks to others. Like the QRM, the presumption alternative would ultimately harm minorities, people with lower incomes, and first-time homebuyers. These effects would occur because:

(1) The mix of uncertainty about how a presumption might be resolved and available attorneys' fees would invite more extensive litigation than necessary – this will result in far greater costs being borne by all borrowers; and

(2) As a result of the threat of litigation, some lenders will act more conservatively than is necessary to meet the presumption's standards, not extending credit to borrowers who might otherwise qualify; there is real concern that some lenders may gravitate to only originating loans meeting QRM requirements.

MBA would support a safe harbor along the lines proposed by the Board, with certain adjustments to the points and fees calculation. In fact, MBA would support even stricter standards than those proposed by the Board as long as the standards are part of a clear safe harbor. Such standards might include the standards proposed to satisfy the general ability to repay standard, the presumption of compliance as well as the standards proposed for the general QM safe harbor.

We note, however, how a safe harbor is constructed is as important as the establishment of a safe harbor itself. For a safe harbor to be effective, both to guide behavior and to efficiently resolve cases in court, it must be comprised of bright-line standards, the performance of which can be evidenced by the four corners of mortgage and mortgage-related documents. A mortgage agreement, for example, could demonstrate that it does not include prohibited product features. A manual checklist and calculation sheet based on reliable third party standards or output from a recognized automated system(s) could demonstrate that underwriting standards have been followed.

The rules that ultimately emerge must allow a creditor and assignee to demonstrate compliance with the safe harbor standards with certainty, with written and/or automated compliance tools using physical or electronic records that may include: (1) the borrower's written signed application; (2) creditor or assignee's worksheets; (3) third party records;[11] (4) evidence of use of a widely accepted standards such as FHA or

[11] *Third-party record* means—

GSE guides; and/or (5) evidence of use of third-party automated systems, as appropriate, such as DU® or LP®. We emphasize that while final rules should ensure complete documentation and verification of borrower data, the requirements should not simply mandate a cumbersome manual origination process.

If litigation risks are not channeled into a clear determination of whether the standards have been complied with, they risk shutting down credit entirely. This has been the experience with the Home Ownership and Equity Protection Act (HOEPA) provisions. Because of HOEPA liability, concerning high-cost loans, HMDA data demonstrates that only approximately one-tenth of one percent of loans exceeded the HOEPA triggers for the years 2004-2009.[12]

Points and Fees

MBA believes the three percent limit on points and fees requires significant adjustment.

First, based on data that has been developed by lenders, the definition of smaller loans demanding an adjustment should be increased to $150,000.

Second, whether the customer chooses to use an affiliated provider of the lender or not, the bona fide charges for such non-lender service should be excluded from the calculation. The largest of these fees for title services are "filed fees" over which the lender has no discretion.

Third, while the compensation to originator companies should be excluded from the calculation in light of the recent loan originator compensation rule, at a minimum the payments by borrowers to creditors and brokerages as well as the compensation they in turn permit their originators should not both be counted. Double counting in this manner is simply unfair.

Fourth, MBA supports the other exclusion in Dodd-Frank, including but not limited to certain up-front mortgage insurance premiums and up to two discount points depending on the nature of the rate reduction. MBA will provide further views and documentation on this matter in its comment letter on the QM rule.

(i) A document or other record prepared or reviewed by a person other than the consumer, the creditor, or the mortgage broker, as defined in § 226.36(a)(2), or an agent of the creditor or mortgage broker;
(ii) A copy of a tax return filed with the Internal Revenue Service or a state taxing authority;
(iii) A record the creditor maintains for an account of the consumer held by the creditor; or
(iv) If the consumer is an employee of the creditor or the mortgage broker, a document or other record maintained by the creditor or mortgage broker regarding the consumer's employment status or employment income.
[12] MBA Analysis of HMDA Data, 2011.

QM/QRM

The obvious difference between the QRM and QM proposals is that the QRM would hard wire high numerical down payment and low LTV and DTI requirements into its requirements. While the QM also requires a loan meet strict product restrictions and underwriting requirements, it appropriately does not impose specific numerical down payment, DTI or LTV requirements.

MBA believes that because both the QRM and QM constructs were intended to achieve the same purpose of ensuring better, more sustainable lending, both constructs should be essentially the same. Considering that the QRM restrictions would exclude too many borrowers from the most affordable, sustainable loans, MBA believes the QM proposal is a much better starting point for both sets of rules.

III. SAFE Act

The Secure and Fair Enforcement Mortgage Licensing Act (SAFE Act) is a major part of the new requirements affecting mortgage loan origination that deserves congressional monitoring. SAFE, which was enacted in 2008 as part of the Housing and Economic Recovery Act, establishes two parallel means of qualifying loan originators – one operated by the states and a second one currently operated by federal banking agencies.

SAFE required the states to establish licensing and registration requirements for originators employed by state regulated lenders and mortgage brokers. Under SAFE, HUD was also required to establish a backup licensing and registration system for those states that did not implement their own system by the statutory deadline. In the event a state system does not meet SAFE's minimum requirements, HUD was authorized to impose the backup system. As of this date, all states have established licensing and registration requirements.

Parallel to the state system, SAFE also requires the federal banking agencies,[13] through the Federal Financial Institutions Examination Council (FFIEC), to develop and maintain a system for registering loan originator employees of depository institutions and their owned and controlled subsidiaries regulated by federal banking agencies or the Farm Credit Administration.

[13] Under SAFE Sec. 1502,12 U.S.C. 5103, the federal banking agencies include the Board of Governors of the Federal Reserve System (Federal Reserve), the Comptroller of the Currency (OCC), the Office of Thrift Supervision (OTS), the National Credit Union Administration (NCUA) and the Federal Deposit Insurance Corporation (FDIC).

Under Dodd-Frank, both the back-up functions of HUD and the responsibilities of the federal banking agencies respecting loan originator supervision are to be reassigned to the CFPB.

The Conference of State Bank Supervisors (CSBS) and the American Association of Residential Mortgage Regulators (AARMR), both associations of state regulators, also have been key to implementing the state licensing system. In 2009, these associations developed a model state law that HUD approved – without notice to and comment by the public – setting forth minimum state law requirements.

On June 30, 2011, HUD issued its final rule[14] setting forth the minimum standards for the state licensing and registration of residential mortgage loan originators and requirements for operating the Nationwide Mortgage Licensing System and Registry (NMLSR), and HUD's federal oversight responsibilities pursuant to SAFE.

SAFE requires that registration of both federally regulated and state licensed loan originators be accomplished through the same system, the NMLSR. This system is operated through CSBS and AARMR.

Currently, requirements under the state and federal systems are inconsistent. Loan originators for state licensed regulators must be both licensed and registered. Loan originators for federally regulated lenders, however, must only be registered (because they are subject to federal requirements). Consequently, mortgage originators of federally regulated institutions, no matter how experienced, must go through training yet again and licensure before they can work for and serve customers of state regulated lenders.

At the same time, because SAFE sets only minimum standards for licensing and qualification, state requirements are inconsistent. States have varying education and licensing requirements. Some have imposed credit score requirements for originators that are inconsistent and others have differing educational and testing requirements. Because of these differences, well-qualified mortgage originators cannot serve consumers across state lines until they, too, have met training and other requirements that are essentially redundant.

For all of these reasons, state regulated companies, including smaller enterprises, are disadvantaged in attracting qualified originators from federally regulated lenders. Consumers, in turn, suffer from decreased choices and potentially increased financing costs.

[14] 76 Fed, Reg. 38464 (June 30, 2011)

In 2010, the federal banking agencies issued a final SAFE rule and the Farm Credit Administration concluded its SAFE rulemaking. Among other things, the federal banking agencies' rule concluded that SAFE's definition of "loan originator" generally excludes employees engaged in loan modifications or assumptions and, consequently, such employees of institutions regulated by banking agencies and their subsidiaries will not be required to register with the NMLSR.[15] Some state governments have also concluded that servicers and/or those engaged in loan modifications in some form are not covered by SAFE; others have covered servicers expressly and still others await HUD's final rules.

HUD's proposed rule paradoxically asked whether loss mitigation specialists should be covered under SAFE, but in its June 30, 2011 final rule[16] left this matter for determination to the CFPB.

MBA's Position

MBA has been particularly concerned about a state-by-state approach to licensing resulting in inconsistent requirements, the failure of regulators to lessen the disadvantages that result from asymmetrical requirements under SAFE for federally-regulated versus state regulated lenders, and the extension of SAFE's requirements beyond originators to servicers.

Without revising the statute, MBA believes HUD and eventually the CFPB can do much more to achieve SAFE's central objective of establishing consistent standards for state regulated loan originators, facilitating competition among lenders and the availability nationwide of well-qualified originators. Differences in education and testing requirements among states as well as different requirements for credit scores unduly burden lenders and increase costs while interfering with the movement of qualified originators to serve consumers.

MBA believes the government's efforts going forward should encourage consistency and permit transitional licensing of federally registered originators pending state licensure and the reciprocity of out-of-state licenses. States should establish provisions for transitional licensing of registered loan originators of federally regulated entities, who are required to be registered under SAFE but not licensed, to be licensed for a reasonable period of time, on a transitional basis, while seeking to meet the state licensing requirements. Additionally, when a state has requirements that differ from

[15] The joint final rule as adopted by the FDIC on November 12, 2009 at http://www.fdic.gov/news/board/2009nov12no8.pdf, pp. 24-25.

[16] 76 Fed, Reg. 38464 (June 30, 2011)

those of another state where an originator has been licensed, the state should either recognize the license or, at minimum, provide a transitional license to the out-of-state licensee for a reasonable period of time to permit satisfaction of licensing requirements. If necessary, the statute should be amended to achieve these ends.

Moreover, MBA has consistently taken the position that there is no basis under SAFE or its legislative history to require that mortgage servicer employees be licensed and/or registered. Additional licensure and registration requirements under SAFE for persons engaged in loan modifications or assumptions, as proposed by HUD, will unnecessarily lessen the availability of loan modification specialists and increase servicing costs. Most importantly, such coverage will hamper the ability of loan modification specialists to move between federally and state regulated companies and otherwise hinder servicers' ability to serve the needs of troubled borrowers particularly those facing foreclosure.

MBA hopes the CFPB will conclude the term "loan originator" was not intended to and does not encompass servicers, including those engaged in loan modifications and assumptions. At this point, any other result would not only be harmful to the servicing process, but would add to the asymmetry between federally-regulated and state-regulated entities.

MBA asks Congress to carefully monitor this matter and, if necessary, take steps to exempt servicer employees engaged in loan modifications from SAFE coverage. Notably, following the enactment of SAFE, servicers engaging in loss mitigation activities were excluded from the definition of "originator" under Dodd-Frank by Congress – for good reason.

Congress should also carefully monitor the other activities of the CFPB with respect to SAFE. Such monitoring should seek to ensure that SAFE is implemented in a manner that serves its purpose of providing sound, consistent qualification and registration standards across the nation for mortgage loan originators, while also fostering a level playing field between federally-regulated and state-regulated lenders to further competition and best serve consumers.

The system should (1) allow qualified loan originators to move among the states and among federally-regulated and state-licensed lenders; (2) further consistency among the states; and (3) not diminish its focus by extending unnecessarily into areas such as licensing of servicers. Congress should also ensure that the NMLSR operates as economically and efficiently as possible.

IV. LOAN ORIGINATOR COMPENSATION

During the past 18 months, two government agencies took separate actions that resulted in considerable implementation and operational costs for the mortgage industry – costs that are ultimately borne by consumers. These actions included an unanticipated and abrupt policy reversal by the Wage and Hour Division of the Department of Labor (DOL) rendering the "administrative exemption" to the Fair Labor Standards Act (FLSA) largely unavailable to mortgage loan officers,[17] as well as a final rule issued by the Federal Reserve broadly prohibiting certain longstanding compensation practices for mortgage loan originators.[18]

DOL Wage and Hour Division's Ruling

On March 24, 2010, the Acting Director of DOL's Wage and Hour Division issued an Administrative Interpretation (AI) holding that employees who perform the typical job duties of a mortgage loan officer do not qualify as *bona fide* administrative employees within the "administrative exemption" under the FLSA. This action abruptly reversed and withdrew a September 8, 2006, opinion to the MBA from the Wage and Hour Division permitting use of the administrative exemption for loan officers. The AI was issued without notice or public comment and with no time for lenders to implement the new requirements. This abrupt reversal is subjecting the industry to unnecessary litigation seeking significant alleged damages.

Employees paid on commission outside the mortgage industry are ordinarily exempt from FLSA coverage under a "retail sales" exemption, which has not been available to financial services employees. A relatively antiquated Supreme Court decision created this anomaly. For financial services employees to be exempt, another exemption – such as the "administrative exemption" or "outside sales exemption" – must apply. Forcing mortgage loan officers to be covered under the FLSA is necessitating additional administrative and reporting requirements in addition to inviting litigation that will increase costs to companies and ultimately consumers.

On January 12, 2011, MBA filed suit against DOL under the Administrative Procedure Act (APA) asking the United States District Court for the District of Columbia to set aside the AI. MBA's position is that when an agency reverses its interpretation of its own regulations, the law requires that the new interpretation be issued only after notice and an opportunity for public comment. Because this public process was not followed, the AI should be set aside. Also, because the DOL's interpretation in the AI is contrary

---

[17] Administrator's Interpretation No. 2010-1 (AI).

[18] 75 Fed. Reg. 58509, (September 24, 2010).

to the plain language of the DOL's regulations and the preamble interpreting them, MBA's suit urges that the AI be considered arbitrary, capricious, an abuse of discretion, and otherwise contrary to law in violation of the APA.

Recently, a U.S. District Court jury found for the lender in a major case involving the company's use of the administrative exemption. The verdict is consistent with MBA's view that overtime requirements are inapplicable to those professionals who advise consumers on mortgage loans and also consistent with DOL's 2006 opinion.

Federal Reserve's Loan Originator Compensation Rule

In 2009, as part of an overhaul of its Truth in Lending Act (TILA) disclosure rules,[19] the Federal Reserve proposed restrictions on loan originator compensation to prohibit unfair and deceptive acts and practices. It did not move forward with its overhaul of disclosures, but in August 2010 finalized the loan officer compensation proposal, knowing that additional rulemaking would be needed to implement similar and additional rules under Dodd-Frank.

The Federal Reserve rule prohibits: (1) basing compensation to a loan originator on a loan's terms or conditions, subject to an exception for loan amount; (2) compensation to a loan originator from both the consumer and a party other than the consumer for the same transaction; and (3) an originator from steering a consumer merely to receive greater compensation. It appropriately does not subject payments from the secondary market to lenders or mortgage brokers to the originator compensation restrictions where they are funding loans through deposits or warehouse lines of credit. On the other hand, it subjects creditors as well as brokerages to the rule's steering restrictions when they are simply brokering loans.

MBA opposed the Federal Reserve's loan originator compensation rule when it was proposed and favored a far more targeted approach that included better disclosure. It also opposed piecemeal rulemaking on this subject knowing these rules would be revised later under Dodd-Frank.

Moreover, since the rule was issued, countless compliance questions have arisen from creditors and loan originators. These include such very basic questions such as: What defines an 'originator'? What justifies compensation differences among products? How do the rules work with state financing programs? And how is the rule to be reconciled with the RESPA rules? The rule and its accompanying commentary did not provide clear answers to numerous important questions. While the Federal Reserve provided some verbal responses to industry questions, it made clear that only written

[19] Cite 2009 Rule

commentary could be relied on and it would not provide such clarification outside the rulemaking process prior to the rule's effective date. At the same time, many of the answers that were provided were inconsistent with the rule itself and its purposes.

MBA spent considerable time and resources seeking and providing industry guidance on the rule for its members through numerous workshops and webinars, one of which the Federal Reserve participated in. Despite continuing uncertainty, the Federal Reserve maintained its compliance deadline of April 1, 2011, for loan applications received by creditors, giving lenders less than seven months to comply.

MBA's Position

DOL Wage and Hour Division's Ruling

MBA would support legislation, if necessary, to require that DOL withdraw its Administrative Interpretation. If DOL determines, following a study of the industry, that a change in its interpretation is warranted, it should propose any revision to its 2006 interpretation for public comment. Following consideration of public comments, if DOL still determines to go forward, a sufficient period to implement the rules should be authorized before any new interpretation becomes effective.

Federal Reserve's Loan Originator Compensation Rule

Congress should carefully monitor the CFPB's implementation of the Federal Reserve's loan originator compensation rule and insist on a review of its guidance. MBA also believes Congress should carefully monitor the upcoming implementation of the Dodd-Frank provisions on loan originator compensation, to ensure that sufficient input is received from and appropriate compliance guidance is provided to lenders.

While some of the Dodd-Frank restrictions in this area overlap with recent actions by the Federal Reserve, we are very concerned about how the new anti-steering provisions will be implemented and that the follow-on rules provide an opportunity for us to correct those aspects of the Board rules that are ill-founded.

A larger point is that as responsibility for TILA and broad consumer financial regulation moves to the CFPB, it is particularly important for the CFPB to develop an orderly process for its myriad rulemaking initiatives – not only to ensure meaningful input from the industry and other key stakeholders, but to develop well-conceived rules and a process for providing timely, reliable guidance well prior to implementation.

V. APPRAISALS

MBA has long encouraged efforts to require residential property valuation practices that minimize opportunities for fraud, coercion or undue influence in the loan approval process. MBA continues to support provisions in Section 1472 of Dodd-Frank and policies outlined in the Federal Reserve's Interim Final Appraisal Rule, which became mandatory on April 1, 2011. Key provisions in the statute and the rule include maintaining appraisal independence and requiring appraisers to be paid "customary and reasonable fees."

These compliance provisions comport with many of MBA's principles for fostering the validity of property valuations and ensuring the integrity of those who conduct such valuations. MBA strongly endorses policies to ensure that appraisers conduct property valuations in a manner that is free from the influence of any party to a real estate transaction that has a financial interest in its outcome, including real estate agents, title agents, mortgage brokers, loan officers, sellers and buyers. Allowing a party with a material interest in the successful origination of the transaction to influence an appraiser hinders what must be an arms-length collateral valuation process and jeopardizes "appraiser independence" Itself. This independence is critical to protecting the lender and the borrower from valuations that misrepresent the true market worth of a property.

With respect to the provision regarding "customary and reasonable" fees, MBA strongly agrees with the Board's determination that the marketplace should be the primary determiner of the value of appraisal services. The method proposed by the Board in the rule is logical, fair, and objective. It best protects consumers from excessive fees and allows the marketplace to find and create efficiencies which ultimately result in lower consumer borrowing costs.

MBA's Position

One area of concern is the proliferation of legislative activity in the states regarding the regulation of the appraisal industry and appraisal management companies (AMCs). Many states are considering various legislative proposals aimed at dictating how appraisal/vendor management companies should operate their businesses. Increased legislative activity over the last year has resulted in a myriad of laws that have unnecessarily increased the regulatory burden on lenders as national and regional companies try to ensure compliance with often conflicting state regulations. Recent proposals for appraisal/vendor management company laws in numerous states present conflicts of interest and inconsistencies and would bring unintended consequences. Many of these proposals would neither improve the industry or safeguard the consumer

In an effort to provide reasonable and effective oversight and consistent policies, MBA recommends the regulation of appraisal valuation standards by a strong, single, federal entity, rather than a patchwork of state laws where separate and conflicting state requirements create confusion and costly compliance burdens.

MBA believes that strong, uniform national supervision of the appraisal industry is critical to achieving consistently high standards. A possible regulator could be the Appraisal Subcommittee of the Federal Financial Institutions Examinations Council (FFIEC). Effective national regulation would assist in rebuilding trust and confidence in the appraisal and mortgage industries and provide protection from unscrupulous actors who taint the home buying process and place both lenders and consumers at financial risk. Your support of such legislation would be welcome.

VI. RESPA-TILA

Under Dodd-Frank, the CFPB takes over responsibility for RESPA and TILA along with numerous other consumer financial protection laws. The law also mandates that no later than one year after the transfer date, the CFPB issue a proposed regulation to integrate and combine the TILA and RESPA disclosures at application and at settlement.

MBA has long supported much greater transparency in the mortgage process and comprehensive reform of RESPA and TILA disclosures. For that reason, we welcome Dodd-Frank's consolidation of RESPA and TILA authorities under one roof. Recent experience has shown that separating these authorities between HUD and the Federal Reserve did not result in improvements to these disclosures.

We also strongly support Dodd-Frank's mandate to integrate RESPA and TILA disclosures and the effort by Treasury Secretary Timothy Geithner and Special Advisor to the President Elizabeth Warren to make this work a high priority of the CFPB. Generations ago, Congress enacted RESPA, as HUD's responsibility, largely to ensure consumers were informed of their real estate settlement costs and TILA, as the Federal Reserve's responsibility, to ensure consumers are informed of the costs of credit. Considering that the purchase and financing of a home is the largest single financial transaction for most people, and that closing costs are intertwined with credit costs, both sets of disclosures must be effective, well coordinated and complementary.

Since these laws were enacted, in part because of the divided responsibility for regulation, RESPA and TILA disclosures have gone in different directions and are accompanied by confusing and sometimes overlapping requirements.[20]

[20] A recent example of overlapping and problematic TILA and RESPA requirements is the new Interim Final Regulation (MDIA) issued by the Board of Governors of the Federal Reserve System (Board) under the recent

Although both agencies have recognized the need for reform, they moved separately in that direction with disappointing results. In 2008, HUD proposed and finalized rules overhauling the Good Faith Estimate (GFE) and HUD-1 Settlement Statement. Untold expenses continue to be incurred by the lending industry to implement that rule, which at this point is likely to be eclipsed by new comprehensive reforms.

In the summer of 2009, as indicated earlier, the Board proposed a complete overhaul of its TILA disclosures for most closed-end and open-end transactions and required comments at the end of that year. The following summer, the Board issued a second proposal covering transactions and topics not addressed the previous year. While there are good ideas in these proposals, both proposals required extensive review and an enormous investment of time by stakeholders to provide meaningful comment. Ultimately, however, the Federal Reserve indicated it would not finalize most of the proposals so as not to interfere with the upcoming CFPB effort. It is possible that the CFPB may reawaken some of these ideas but we believe it should only do so in the context of comprehensive reform and a new opportunity for comment.

Notably, Congress added to disclosure concerns in 2008 by requiring new requirements for TILA disclosures, which differ from the requirements and timing of RESPA disclosures. These differences were exacerbated by additional timing requirements for redisclosure of the GFE under the new RESPA rule, and proposals in the previous Congress for additional timing requirements would have made matters worse.

As a result of both legislative and regulatory requirements, consumers today receive a package of disclosures when they apply for a loan, and then continue to get a dizzying array of redisclosures and amended disclosures until their loan closes. A comprehensive look at all of the timing requirements for disclosures should occur along with the effort to redraft the disclosures themselves.

In May of this year, the CFPB's effort began with announcement of an iterative process for proposing and refining prototypes of forms combining existing RESPA and TILA disclosures over the coming months to culminate in a final set of proposed forms and issuance of accompanying rules. The first set of prototypes was issued then and

---

Mortgage Disclosure Improvement Act. This rule requires disclosure of a new Interest Rate and Payment Summary form to show how an interest rate or payment amount may change. We agree disclosure of that information is important. But the new disclosure form repeats information that is already required to be disclosed on the GFE and HUD-1 under the new RESPA rule, but on a different form.

comments were invited for a week. A revised set of prototypes were issued at the end of June with a week-long comment period over the July 4th break.

While MBA appreciates that the process is moving forward, we are seeking clarification from the CFPB regarding the extent to which the forms will be governed by current RESPA and TILA requirements. That information is needed so that input by the industry and other stakeholders can be focused. MBA recently requested a meeting with the CFPB to clarify this issue and to offer an opportunity for more robust input into the process from experienced professionals.

MBA's Position

MBA believes that while this effort needs to be encouraged, Congress should monitor the CFPB's RESPA and TILA efforts carefully. MBA opposes implementing piecemeal changes to RESPA and TILA disclosures. Rather, we believe the CFPB should conduct comprehensive reforms and issue a proposed rule that includes the required simplification of RESPA and TILA disclosures mandated by Dodd-Frank.

MBA believes it is crucial that the CFPB draw on the experience of the housing finance industry as it develops its proposals. Lenders work with consumers day-in and day-out and have extensive experience in conveying information to consumers in the most useful manner at optimal times.

When the CFPB completes its proposal, it must provide sufficient opportunity for comment and deliberation. The CFPB should not implement revisions without providing both formal and informal guidance so lenders large and small can comply. Also, considering the extensive systems, retraining, legal and other costs that these changes will require – the costs of which will ultimately be borne by consumers – a reasonable period for implementation is essential.

Finally, while Congress should monitor the process, we would urge it to refrain from amending either the TILA or RESPA requirements at least until the direction of the CFPB's effort becomes clear. Premature legislative action would only serve to further confuse an already confusing process.

Conclusion

We appreciate the efforts of this subcommittee to examine these important regulations and consider our comments. No matter how well intentioned rules may be, they cannot be allowed to harm American families, the mortgage market or the nation's economic recovery. Thank you again for providing me the opportunity to testify. I look forward to your questions.

Real Estate Valuation Advocacy Association (REVAA) and Coalition to Facilitate Appraisal Integrity Reform (FAIR) Joint Testimony

Presented by
Don Kelly, Executive Director of REVAA

Before the House Financial Services Committee, Subcommittee on Insurance, Housing, and Community Opportunity hearing on Mortgage Origination: The Impact of Recent Changes on Homeowners and Businesses

July 13, 2011

STATEMENT OF DON KELLY BEFORE THE SUBCOMMITTEE ON INSURANCE, HOUSING, AND COMMUNITY OPPORTUNITY OF THE HOUSE COMMITTEE ON FINANCIAL SERVICES

July 13, 2011

Introduction and Summary

I am Donald E. Kelly, Executive Director of the Real Estate Valuation Advocacy Association ("REVAA"). I appreciate the opportunity to provide testimony on behalf of REVAA and the Coalition to Facilitate Appraisal Integrity Reform ("FAIR") for the Insurance, Housing, and Community Opportunity Subcommittee's hearing on "Mortgage Origination: The Impact of Recent Changes on Homeowners and Businesses."

With this testimony, I aim to:

1) provide the Subcommittee with information about the important role that REVAA and FAIR members play in the valuation industry and the valuable services they provide in the course of a residential real estate appraisal;

2) discuss REVAA's and FAIR's proactive efforts to work collaboratively with states to implement registration and regulatory requirements for appraisal management companies ("AMCs");

3) provide insight from our industry regarding the regulatory implementation of the "customary and reasonable" compensation requirement contained in the Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank Act"); and

4) offer our industry experience and expertise as a resource to the Subcommittee as you continue your efforts to reform the mortgage origination process.

Background/Benefits of Working With an AMC

REVAA is a real estate valuation industry trade association that promotes education, high ethical standards, political awareness, and the professional development of the real estate valuation industry.

REVAA believes that homeowners, the mortgage lending industry, and the economy as a whole are best served by a diversified array of real estate valuation products. With growing complexity regarding real estate valuation in today's challenging market, it is vital that end-users have the ability to select the most appropriate valuation service to meet their specific needs.

REVAA members have committed to being proactive in efforts to promote and expand the industry. Our members produce and deliver real estate valuation products including Appraisals, Broker Price Opinions (BPOs), Automated Valuation Models (AVMs), and other innovative valuation methods that benefit mortgage investors, servicers, originators, and borrowers.

FAIR is a coalition of five of the nation's largest AMCs,[1] which operate networks of individual appraisers and appraisal firms for the completion of appraisal reports.

AMCs operate regional and national networks of employee appraisers, independent contractor appraisers, and appraisal companies/firms for the completion of appraisal reports. They act as a centralized appraisal source for mortgage lenders that operate on a wide geographic basis. Rather than contacting hundreds of individual appraisers in each state or jurisdiction, a lender may obtain appraisals through a centralized AMC model. The AMC then works to match the assignment with a qualified, local market appraiser based on numerous factors. The selected appraiser then performs the physical inspection of the property and issues an appraisal report containing the appraiser's opinion of property value. The AMC performs extensive quality control functions on behalf of both the appraiser and the lender to ensure a high quality appraisal report is delivered to the client. Prior to the use of AMCs, there was typically little/no quality control performed prior to the delivery of the appraisal report.

There are significant benefits for both an appraiser and a lender when they work with an AMC. The lender hires an AMC to act on its behalf to maintain an appraiser panel, engage a real estate appraiser, perform the administrative functions involved in the appraisal ordering, tracking, and delivery process, perform quality control functions on behalf of both parties, and handle the invoicing and payment of the appraiser. AMCs are able to provide the highest level of appraiser independence by acting as a firewall between a lender and an appraiser as a neutral third party. In addition to these services, AMCs also have created and/or provided technological innovations in the appraisal industry, including the development of electronic appraisal delivery and the development of supplemental addendums and products to complement the current standardized appraisal forms. AMCs have also provided expertise in the development of the MISMO XML standards and other "landmark" technological developments in the appraisal industry over the past 15 years.

An appraiser benefits from working with an AMC by having an advocate to ensure that no inappropriate or improper attempt is made to influence the appraiser process. Appraisers rely on AMCs to handle marketing, perform panel management, and provide for the efficient payment of appraisal fees. This allows appraisers the opportunity to spend more time actually appraising as opposed to performing the back-office work that is associated with the appraisal profession. In addition to these services, AMCs provide extensive quality control support, which reduces the time that appraisers spend fixing errors and resolving underwriting suspensions and helps to limit appraisers' buyback exposure. The majority of appraisers are individual

[1] These five AMCs include: (1) LSI, a division of Lender Processing Services, Inc.; (2) ServiceLink Valuation Solutions, LLC, a Fidelity National Financial, Inc. company; (3) Valuation Information Technology, LLC d/b/a Rels Valuation; (4) CoreLogic, Inc.; and (5) PCV/Murcor. Rels Valuation is an affiliate of CoreLogic, Inc. and Wells Fargo Bank.

proprietors who have no realistic ability – other than through AMCs – to benefit from having third-party quality control processes performed on their appraisal reports.

In addition to the benefits provided by AMCs to appraisers and lenders, it is important to also note the benefits enjoyed by consumers when an appraisal is procured by a lender through an AMC. The AMC model, which has been utilized by many large lenders for over twenty years, provides efficiencies to the appraisal process that allow mortgage transactions to close in less time and help ensure that services are performed at competitive, market-based prices. The success of the AMC business model has been seen throughout the industry with the result being that nearly 70% of all residential appraisals ordered and produced nationwide are provided through an AMC. Government entities (*e.g.*, the Federal Housing Administration or "FHA") have also recognized the presence and importance of AMCs in the appraisal industry and have provided specific guidance to lenders that utilize AMCs (*e.g.*, Mortgagee Letter 2009-28).

Overview of AMC Functions

AMCs not only manage networks of independent, third-party service providers, but they manage all of the ordering, tracking, quality control and delivery tasks associated with the appraisal process. Below are some of the specific functions that an AMC provides:

- Recruit and qualify vendors for their networks, by verifying appraisal licensure and/or certification, checking references, performing background checks, performing examinations, and auditing work samples;

- Negotiate service level expectations and maintain service level agreements with individual vendors;

- Assume loan-level administrative duties for the large numbers of transactions in their pipelines, including (i) performing order entry and assignment, (ii) tracking order status, (iii) updating clients on delays, (iv) performing both pre- and post-delivery quality control, (v) transmitting preliminary and final hard copies of appraisal reports to clients, (vi) handling accounts payable and receivable, (vii) engaging in dispute resolution between lenders and appraisers, (viii) providing and administering warranties and errors and omissions insurance, and (ix) ensuring proper record retention;

- Provide a single point of contact for lenders and uniformity across jurisdictions;

- Offer advanced technology interfacing specializing in the assignment, tracking, and reviewing of appraisal reports and the electronic delivery of reports consistent with the needs of the lender and/or investor; and

- Warrant the quality of the final appraisal product to supplement the errors and omissions insurance carried by appraisers.

The Dodd-Frank Act State Registration and Regulatory Requirements

AMCs are subject to multiple regulatory requirements. First, existing banking regulatory standards are imposed on AMCs as the agents of federally regulated banks and lenders. Second, AMCs are subject to registration requirements and other standards of conduct under state laws. Third, AMCs are the subject of new regulatory requirements, including new minimum standards and a national registry applicable to AMCs under the Dodd-Frank Act. Finally, because mortgage lenders are the AMCs' clients, any appraisal reforms targeted at lenders also have a direct effect on the operations of an AMC.

The Dodd-Frank Act amends the Financial Institutions Reform, Recovery and Enforcement Act of 1989 to require the federal Appraisal Subcommittee to monitor the requirements established by states to register and supervise the activities of AMCs.[2] The Dodd-Frank Act requires the federal banking agencies to jointly, by rule, establish minimum requirements to be applied by a state in the registration of certain AMCs, including a requirement that AMCs (except a subsidiary which is owned and controlled by a federal financial institution) be registered and regulated by a state appraiser board, a requirement that AMCs verify that only licensed or certified appraisers are used for federally-related transactions, a requirement that AMCs require appraisals to comply with Uniform Standards of Professional Appraisal Practice, and a requirement that AMCs require appraisals to be conducted independently and free from inappropriate influence in accordance with Section 129E of the Truth in Lending Act ("TILA").[3]

Prior to the passage of the Dodd-Frank Act, several states had begun the process of enacting AMC laws to require the registration of AMCs, to establish appraisal independence standards applicable to AMCs, to set minimum education and licensing requirements for certain employees of AMCs, to provide for the disclosure of appraisal and appraisal management fees within an appraisal report, and to authorize state appraisal boards or other state agencies to enforce the state AMC laws. Many of these states either already encompassed the minimum standards that are in the Dodd-Frank Act or are now in the process of amending their laws to ensure they reflect the minimum standards enumerated in the Dodd-Frank Act. Other states continue to introduce proposed legislation to provide for the registration and supervision of AMCs. Currently, 29 states have enacted such laws and an additional six states have such laws pending.

AMCs have been actively involved with the states from the inception of these registration laws and have long supported transparency and independence in the appraisal process and the registration of bona fide AMCs. AMCs also are working proactively and collaboratively with state regulatory agencies to craft regulations to implement these laws and ensure that the most effective processes are in place to achieve the goals of the registration laws. AMCs provide valuable services in the course of a real estate appraisal, and it is important to us that appraisals are ordered from reputable and sound AMCs that are committed to transparency in the process, full compliance with all registration laws, and delivering the highest-quality appraisal products.

---

[2] *See* the Dodd-Frank Act, Pub. L. No. 111-203, § 1473(f)(1) (2010).

[3] *See id.* § 1473(f)(2).

We also believe it is important to work towards consistency and uniformity in state AMC laws and regulations to ensure that AMCs can effectively implement the necessary compliance procedures to operate on a national basis. We will continue to support the states' efforts to implement reasonable and appropriate laws and standards to better the appraisal industry.

The Dodd-Frank Act "Customary and Reasonable" Appraiser Compensation Requirements

As noted above, AMCs provide valuable services to various parties in the appraisal process. AMCs have contractual agreements with lenders and are compensated by the lender for the appraisal and the AMC services. The fees are combined on the HUD-1 appraisal statement as dictated by the Real Estate Settlement Procedures Act, which permits the appraisal fee to include both services. The government-sponsored enterprises (Fannie Mae and Freddie Mac) and the Department of Housing and Urban Development both recognize that AMCs are key factors in the market and have provided guidance to lenders on the use of AMCs (*see* Mortgagee Letter 2009-28).

The Dodd-Frank Act amended TILA by adding Section 129E to require adherence to appraisal independence standards and also to require that lenders and their agents (including AMCs) compensate appraisers at a "customary and reasonable" rate for appraisal services in the market area of the property being appraised. The Dodd-Frank Act also provided that "evidence for such fees *may* be established by objective third-party information, such as government agency fee schedules, academic studies, and independent private sector surveys." (Emphasis added.) Fee studies, however, are required to "exclude assignments ordered by known appraisal management companies." [4]

The Federal Reserve Board ("Board") was charged with promulgating interim final regulations to implement Section 129E. These interim final regulations became effective April 1, 2011. The Board established two alternative presumptions of compliance for lenders and their agents to satisfy this requirement.

REVAA and FAIR believe that the appraiser compensation standards promulgated by the Board are in compliance with the Dodd-Frank Act, and they reflect the variations in actual services and other factors that exist in the marketplace. Appraisal services are not one-size-fits-all, and we believe the Board has created a compliance structure for the payment of "customary and reasonable" appraisal fees that reflects market realities and ensures that prices paid by consumers will remain competitive.

The first presumption permits lenders and their agents to rely upon recent rates actually paid for appraisal services (including rates paid by AMCs) in the relevant geographic market, adjusted as necessary to account for six other factors such as type of property or scope of work. Although the term "customary and reasonable" was undefined in the Dodd-Frank Act, the Board recognized that the Dodd-Frank Act language is identical to HUD's requirement obligating FHA lenders to ensure that appraisers are paid "at a rate that is customary and reasonable for appraisal

[4] *See* Section 129E(i)(1) of TILA.

services performed in the market area of the property being appraised." Consistent with HUD's approach within Mortgagee Letter 2009-28, the Board concluded that the marketplace should be "the primary determiner of the value of appraisal services, and hence the customary and reasonable rate of compensation for fee appraisers."

The second presumption permits reliance on objective third-party information, including fee schedules, studies and surveys prepared by independent third parties such as government agencies, and academic institutions and private research firms, provided they are based on recent rates paid to a representative sample of appraisers in the geographic market of the property being appraised (but excluding compensation paid to appraisers for assignments ordered by an AMC).

REVAA and FAIR believe that the Board correctly implemented Congress' plain language and intent by establishing two presumptions – one that relies on the recent rates actually paid in the marketplace and one that relies on objective third-party fee surveys that exclude fees charged by AMCs. There are currently very few third-party fee surveys in the marketplace, none are comprehensive enough to include all of the differences in geographic areas/markets, and they do not fully encompass all of the appraisal products offered by AMCs.

We understand that the Board does not plan to issue a "final" rule before its rulemaking authority is transferred to the Consumer Financial Protection Bureau ("CFPB"). While the interim final rule remains effective without such "finalization," AMCs are concerned that some appraisers may seek reconsideration by the CFPB with the intention to mandate a higher level of compensation for appraisers than is supported by current market rates. Under this scenario, consumers would be subjected to higher appraisal fees that would often exceed the market rate and would not be gaining additional services for these higher fees. Furthermore, guaranteeing a higher fee for appraisers would not ensure better performance, as experience has shown that higher appraisal fees do not necessarily correspond to higher quality appraisals. Appraisers are required by the Uniform Standards of Professional Appraisal Practice to ensure that appraisals meet minimum requirements regardless of the fee or the nature of the assignment.

Prior to recent regulatory reforms, higher appraisal fees were the custom for many appraisers who, in partnership with overzealous mortgage brokers and lenders, produced appraisal reports that were impacted by inappropriate influence and coercion. The resulting appraisals often reflected inflated values, which certainly did not constitute "high quality" appraisals. The members of REVAA and FAIR respectfully suggest that the Board, the CFPB, and Congress should resist calls from those appraisers to mandate increased rates for appraisals as opposed to allowing the marketplace to dictate appraisal rates.

In addition to the items discussed previously regarding the potential negative impacts on consumers by mandating a higher level of compensation, it is also important to note that there is no single standard or uniform price for appraisals throughout the country. Instead, appraisal fees are set by the competitive marketplace and reflect variations in the scope of work performed by appraisers, the nuances of individual transactions, such as the type and location of the property, the costs associated with producing appraisals in different markets, how quickly the lender has required the report, and the appraiser's level of efficiency in performing an assignment.

Indeed, while Section 129E(i) of TILA provides that lenders and their agents may generally rely on fee studies created by objective third parties to form the basis for "customary and reasonable rates," no reliable and objective fee studies exist across the appraisal spectrum. In fact, two studies that are referenced most actively in the appraisal community to support uniform higher fees demonstrate significant difference between fees within those two surveys for the same areas, do not represent the appraisal industry as a whole, and do not account for the fact that appraisals have multiple uses and multiple markets. Further, we are concerned that undue reliance on fee studies may result in increased collusion among some appraisers to set their fees at artificially high rates, thus influencing fee studies in their area and ensuring that inflated appraisal prices are paid for years to come. In fact, we are already seeing an increasing trend towards price-fixing among appraiser groups in certain states.

The AMC model is a prime example of why a link between higher fees and higher quality appraisals is not a realistic representation of the market. Notably, because of the services and many efficiencies provided by AMCs on behalf of individual appraisers, appraisers are willing to set their appraisal prices at a lower rate for orders accepted from AMCs due to the benefits an appraiser received by working with an AMC. Additionally, AMCs go to great lengths to ensure that only the most qualified and experienced appraisers belong to their networks, with many relationships existing over a 10-15 year period or longer. Appraisers recognize and utilize the extensive quality control processes provided by AMCs to increase the quality of appraisal reports that they produce. Accordingly, while appraisers may set their prices lower when utilizing AMCs, AMCs produce high quality appraisals by ensuring that inappropriate influence does not occur during the appraisal process and by having multiple layers of quality control.

We hope that the CFPB, in issuing final regulations to implement the appraiser compensation standards required by the Dodd-Frank Act, will maintain the compliance structure for the payment of "customary and reasonable" appraisal rates that the Board established.

Conclusion

Thank you for the opportunity to provide testimony and insight in support of the important work of Congress. REVAA and FAIR members play an important role in the housing market, and we hope that you will continue to look to us as a resource going forward.

TESTIMONY OF

ANNE BALCER NORTON

DEPUTY COMMISSIONER

MARYLAND OFFICE OF THE COMMISSIONER OF FINANCIAL REGULATION

On behalf of the

CONFERENCE OF STATE BANK SUPERVISORS

On

"MORTGAGE ORIGINATION: THE IMPACT OF RECENT CHANGES ON HOMEOWNERS AND BUSINESSES"

Before the

INSURANCE, HOUSING AND COMMUNITY OPPORTUNITY SUBCOMMITTEE

COMMITTEE ON FINANCIAL SERVICES

UNITED STATES HOUSE OF REPRESENTATIVES

Wednesday, July 13, 2011, 2:00 p.m.

Room 2128 Rayburn House Office Building

INTRODUCTION

Good afternoon, Chairman Biggert, Ranking Member Gutierrez, and distinguished Members of the Subcommittee. My name is Anne Balcer Norton, and I serve as the Deputy Commissioner of the Office of the Commissioner of Financial Regulation for the State of Maryland.

Maryland's Office of the Commissioner of Financial Regulation (Office) is part of the Maryland Department of Labor, Licensing and Regulation, which is led by Secretary Alexander Sanchez. The Office, headed by Commissioner Mark Kaufman, is responsible for chartering and regulating 63 state-chartered depository institutions including banks, credit unions, and trust companies. In addition, the Office licenses and regulates approximately 10,000 non-depository financial institutions and individual service providers, including mortgage lenders, brokers, servicers and loan originators, consumer loan companies, money transmitters, check cashers, installment loan lenders, credit services businesses, sales finance companies, consumer debt collection agencies, and debt management service providers. The Office conducts periodic examinations of entities under its supervision, responds to consumer complaints, and undertakes enforcement actions to ensure compliance with Maryland law.

It is my pleasure to testify before you today on behalf of the Conference of State Bank Supervisors (CSBS). CSBS is the nationwide organization of banking regulators from all 50 states, the District of Columbia, Guam, Puerto Rico, and the U.S. Virgin Islands. State banking regulators supervise over 5,600 state-chartered commercial banks. Further, the majority of state banking departments also regulates a variety of non-bank financial services providers, including mortgage lenders. For more than a century, CSBS has given state supervisors a national forum to coordinate supervision of their regulated entities and to develop regulatory policy. CSBS also provides training to state banking and financial regulators and represents its members before Congress and the federal financial regulatory agencies.

I thank you, Chairman Biggert, and the Members of the Subcommittee, for holding this hearing on issues affecting residential mortgage origination. State regulators play a central role in overseeing the mortgage origination market, and we appreciate the opportunity to be part of this important discussion.

In my testimony, I will briefly discuss the evolution of the mortgage industry over the past two decades and will speak about the efforts of state regulators to enhance supervision of this industry. Included in my testimony will be a discussion of the Secure and Fair Enforcement for Mortgage Licensing Act of 2008 (SAFE Act) and the Nationwide Mortgage Licensing System and Registry (NMLS), as well as how state regulators conduct supervision of residential mortgage loan originators (MLOs) on a daily basis. Additionally, I will provide state regulators' perspective on some of the specific regulatory topics discussed by other witnesses. Finally, I will discuss some areas of concern to state regulators as we move forward to strengthen supervision of the residential mortgage origination system.

EVOLUTION OF RESIDENTIAL MORTGAGE ORIGINATION

To better understand the current system of mortgage origination, we need to review briefly how we got here. The changes in the residential mortgage industry over the past two decades have been dramatic and far-reaching. Over the past 20 years, the market has ushered in new players, new products, a new originate-to-distribute securitization model, and has had a tremendous impact on the economy as a whole.

This evolution led to a vast flow of liquidity into the mortgage market and increased availability of mortgage credit. But it also brought moral hazard and ultimately, significant harm and financial hardship to many, as the allocation of accountability and risk of a default became muddied through complex arrangements that begin with the local mortgage broker and ultimately end up with a Wall Street investor. Controls that had previously been in place to govern the industry were simply overwhelmed by the evolution and supervision could not keep pace with industry advancements.

STATE REGULATORY RESPONSE TO MORTGAGE EVOLUTION

The policy and regulatory response to the financial crisis remains a work in progress, involving Congress as well as state and federal regulators. State mortgage regulators, concerned about the consequences for communities and consumers of the practices of certain mortgage lenders and brokers, have taken significant action to enhance supervision of the non-depository residential mortgage industry. These efforts have been undertaken with an eye toward maintaining a diverse origination system. State regulators, individually and through CSBS and the American Association of Residential Mortgage Regulators (AARMR), have worked diligently and in an unprecedented manner to create a regulatory system that can support a diverse system of mortgage origination, while still ensuring safety and soundness and consumer protections.

Development and Launch of NMLS

While few may have fully understood the broader risks the radical evolution of the mortgage origination system would have upon the nation's housing finance system, state regulators did see the risks emerging among non-depository mortgage originators. State regulators, who typically have an explicit consumer protection mandate, felt compelled to act to bring greater accountability and transparency to this sector of residential finance that grew so dramatically during the late nineties and into the new century. During the years of 2004 through 2007, while the industry was calling for less regulation, state regulators sought to create a more comprehensive and coordinated supervisory framework to oversee the residential mortgage market and protect consumers.

To that end, NMLS was conceptualized and created by state regulators acting through CSBS and AARMR with the goal to unify state mortgage supervision in a single system that would allow regulators to better coordinate regulation and provide the industry a more uniform licensing process.

The creation of NMLS was a complete transformation of mortgage supervision. NMLS provides the foundation for coordinated, consistent, and comprehensive supervision of the mortgage industry. Prior to the launch of NMLS, there was a great deal of inconsistency in the regulation of the mortgage industry, with licensing and registration standards that varied from state-to-state. NMLS still allows state regulators autonomy, but has now coordinated supervisory processes and documentation.

Perhaps the most critical element introduced by NMLS is the NMLS Unique ID Number. By creating a single system of record shared by separate and sovereign state regulators, NMLS was able to assign each mortgage company, each branch, and each MLO a unique identification number that could be used to track that company, branch, and individual across states and over time. The NMLS Unique ID assists in coordinated state oversight and provides the opportunity for investors and the secondary market to develop better metrics of loan originations and of loan performance.

Further, the NMLS Unique ID has become a central component of the fabric of residential mortgage supervision. The Federal Housing Finance Agency (FHFA) requires Fannie Mae and Freddie Mac to collect the NMLS Unique ID for each loan they purchase. Similarly, the Federal Housing Administration (FHA) requires the NMLS Unique ID for all mortgage loans submitted for insurance. These entities are involved in over 90 percent of the residential mortgage loans originated over the past two years.

The relatively quick adoption of the NMLS Unique ID by mortgage investors and insurers is a testament to the rapid and uniform adoption of NMLS by state agencies. For instance, by October 2010—just 33 months after the launch of NMLS—all 50 states, the District of Columbia, Puerto Rico, and the U.S. Virgin Islands were using NMLS as the system of record to manage their MLO licenses. This is a tremendous demonstration of the states' commitment to coordination and adoption of a new, comprehensive regulatory scheme.

Passage of the SAFE Act

At its launch, NMLS was a voluntary state initiative. Subsequently, Congress, through the leadership of Chairman Bachus, embraced and codified the system into federal law through the SAFE Act, creating an integrated and comprehensive state-federal approach to licensing and registering mortgage lending professions. The SAFE Act certainly helped propel NMLS to the complete supervisory framework it is today. By requiring all states to adopt robust licensing and regulatory standards for state-licensed companies and individuals and mandating registration for federally regulated MLOs through NMLS, the SAFE Act created a coordinated system of state-federal mortgage supervision, while still preserving state autonomy to regulate the mortgage industry.

SAFE Act Implementation and Compliance

After the SAFE Act's enactment, state regulators went to work quickly to implement the law, including development of a model state law to execute the mandates of the SAFE Act in a uniform manner. By July 2009—just one year after the passage of the SAFE Act—49 states, the District of Columbia, and the U.S. Virgin Islands had all passed legislation to bring their laws into compliance with the SAFE Act. This rapid and uniform implementation of a law by so many states was remarkable and demonstrates the commitment and dedication of state officials and state legislatures to enhance supervision of the mortgage industry.

State regulators have moved aggressively to implement the many provisions of the SAFE Act, which include testing requirements, pre-licensure and continuing education requirements, facilitating criminal and credit background checks, providing free public access to licensing information, and creating a mortgage call report.

Since passage of the SAFE Act in July 2008, state regulators and NMLS have:

- Developed and administered the national and state components of the mortgage loan originator licensing test;
- Approved pre-licensure and continuing education courses;
- Implemented a national network of electronic fingerprint capture sites to facilitate processing of fingerprints for required criminal history background checks;
- Created a process for the provision of a single credit report to be used by all relevant state regulators for MLOs licensed in their state;

- Launched www.NMLSConsumerAccess.org, a website for consumers to verify basic information concerning state-licensed MLOs free of charge; and
- Developed the NMLS Mortgage Call Report, which is already beginning to provide timely data on mortgage originations by non-depositories, both at the state and national levels.

One of the main objectives of the SAFE Act was to expand a then state-only initiative into a comprehensive regime covering all mortgage loan originators. To that end, federally regulated MLOs began registering with NMLS on January 31, 2011. This event was the culmination of well over a year's worth of close cooperation between CSBS and the federal banking agencies to modify NMLS in order to provide a system that allows both depositories and individual MLOs to efficiently meet the SAFE Act requirements for registration.

By July 29 2011, all individuals who act as mortgage loan originators and are employed by depositories must be registered on NMLS in order to conduct those activities. The MLOs will have an NMLS unique ID number. Additionally, the depositories that employ these MLOs must also have an account on NMLS and have a NMLS unique ID number. As we near the end of the six-month initial transition period for federally regulated MLOs, over 9,000 institutions and 272,000 individuals have completed the registration process and we anticipate thousands more are working to complete the process.

BENEFITS TO CONSUMERS, POLICYMAKERS, AND INDUSTRY

Information regarding federally regulated MLOs will be available on August 1, 2011 on NMLS Consumer Access (www.NMLSConsumerAccess.org) so that consumers will be able to verify the licensure or registration of all MLOs and their employing company. In other words, just three years after passage of the SAFE Act, nearly every single residential mortgage loan originated in this nation will carry with it the identification of the individual and the company that originated the mortgage. And, through www.NMLSConsumerAccess.org, consumers will have free access to a means for verifying the status and legitimacy of the companies and MLOs they may wish to do business with. This will afford consumers, policymakers, and the industry better transparency about the residential mortgage industry in this country.

Another initiative recently launched that will further improve the amount of information available to policymakers is the NMLS Mortgage Call Report. The NMLS Mortgage Call Report is a quarterly report by companies that hold a state license or registration or employees state-licensed MLOs. One goal is that the NMLS Mortgage Call Report can replace the unique reports that many states currently collect from licensees, thereby providing more efficiency for the industry.

The deadline for the first quarter 2011 NMLS Mortgage Call Report just recently passed and state regulators are busy reviewing this data for accuracy and quality. We believe these reports will provide state regulators more timely information about the activities of their licensees as well as providing policymakers more timely data on the industry as a whole. While data from the NMLS Mortgage Call Report is not yet available, NMLS is providing policymakers better information about the non-depository mortgage origination sector (See Exhibit A).

MARYLAND-SPECIFIC EFFORTS

Maryland completed its transition to the NMLS in December 2010. Currently, there are over 5,100 individual MLOs and over 1,400 mortgage companies licensed in the state of Maryland. All of these companies and individuals were evaluated and approved during the 18-month transition cycle—a massive task. To date, approximately: 60 individual applicants have been denied; 1,950 individual licenses were terminated on January 1 because their license expired; 210 company & branch licenses were terminated on January 1 due to expiration; 360 individuals surrendered their license; 300 companies & branches surrendered their license; 450 individuals voluntarily withdrew their applications; and 50 companies and branches voluntarily withdrew their applications. The significant number of licensees who did not renew in Maryland is consistent with the experience in other states as the non-bank segment of the mortgage industry has contracted in the wake of the mortgage crisis.

Because of our close proximity to those entities we regulate and the local nature of mortgage lending, state regulators are most often best positioned to identify emerging threats and are able to move quickly in response. Accordingly, as foreclosure rates began to rise across the nation in 2007, Maryland Governor Martin O'Malley convened the Homeownership Preservation Task Force, which brought together representatives from the banking and lending industries, federal, state and local government entities, and consumer advocates to study the issue and make recommendations.

The Task Force and its work groups studied the issue, looked at best practices in the industry, and examined laws enacted in other states. The report and recommendations of the Task Force represented broad consensus: all stakeholders at the table were interested in proposals that would reform lending and provide greater protections for consumers. The recommendations resulted in a package of reforms designed to help both those in and at risk of foreclosure as well as comprehensive and common sense credit regulations for mortgage lending practices in the state and providing for more meaningful mortgage licensing requirements including instituting a minimum net worth requirement.

Under Governor O'Malley's leadership, a series of legislative and regulatory reforms enacted in Maryland have included: banning prepayment penalties; assuring a borrower's ability to repay a mortgage loan and verify sources of income; requiring a tangible net benefit in refinance transactions; requiring disclosure on first lien loans to provide borrowers with a notice of housing counseling or homebuyer education available through certified non-profits/HUD-certified institutions; and implementing a duty of good faith and fair dealing by mortgage professionals. Through constant dialogue with both the industry and borrower advocates, the reforms have provided a balanced approached to addressing the overall concerns relating to lending in the state without undue regulatory burden on Maryland licensees.

Prior to 2008, Maryland lacked the necessary regulatory tools needed to combat mortgage fraud. There was no criminal mortgage fraud statute in place and prosecutors were reluctant to bring cases for mortgage fraud relying on general tenets of common law; law that at best, imperfectly fit the crime perpetrated. Legislation was passed to create a criminal mortgage fraud statute to include restitution, forfeiture, enhanced penalties for violations involving vulnerable adults, a private right of action, and a duty for companies to report convictions to any licensing body. During the 2011 legislative session, this law was amended to give the Commissioner authority to issue summary orders directing persons to cease and desist from engaging in alleged violations of this law and to give the alleged offender an opportunity for a hearing. The authority to bring action for such offenses, under the revisions to the Maryland Mortgage Fraud Protection Act, was extended to stop illegal conduct against individuals or companies not licensed by the Commissioner. In other words, the Commissioner is now authorized to address fraud where fraud is found whether or not the perpetrator of such action is licensed in Maryland (MD Code Ann. Real Prop. § 7-401, et seq.). As a result, in fiscal year 2011, our office investigated 264 cases representing more than 1,000 Maryland consumers that had escalated from consumer complaints, 208 of which were mortgage-fraud related resulting in more than 90 Cease and Desist Orders and roughly 30 license revocations.

As we leverage available resources to address mortgage-related fraud, the Maryland Mortgage Fraud Task Force, led by US Attorney Rod Rosenstein, was established in 2009 to unify the agencies that regulate and investigate mortgage fraud and promote the early detection, identification, prevention, and prosecution of mortgage fraud schemes. In addition to our office, participants include the U.S. Department of Justice (DOJ), the Federal Bureau of Investigation (FBI), Maryland's Office of Attorney General, the U.S. Department of Housing and Urban Development (HUD), the Internal Revenue Service, and other state and federal law enforcement and regulatory agencies. The work of the Task Force is evident in a wide-range of indictments, federal prosecution and restitution ordered to aggrieved consumers since its inception.

The goals of the Task Force include: streamlining the procedures for criminal mortgage fraud referrals; developing and implementing a training program for state and federal investigators and prosecutors who handle mortgage fraud cases; sharing useful information with and facilitating cooperation among the many agencies that have a stake in these cases; tracking open investigations to ensure that partner agencies do not duplicate their efforts; pursuing asset forfeiture and securing restitution for victims; and communicating information to the public in order to warn people about common schemes and help prevent them from becoming victims of mortgage fraud and related financial crimes.

This type of cooperation between law enforcement and state regulators on fraud investigation efforts is not unique to Maryland. State regulators across the country have joined forces with the DOJ, the FBI, HUD, and local law enforcement to aggressively combat mortgage fraud. For instance, in April of this year, the Washington state legislature extended its successful mortgage fraud prosecution fund an additional five years. The law requires the collection of one dollar on every mortgage loan closing. This money is set aside in a special account held by the Washington Department of Financial Institutions that funds the costs of criminal prosecution for mortgage fraud. To date, 38 felony convictions can be attributed to this law.

STATE MORTGAGE SUPERVISION

NMLS and the SAFE Act are key parts of a larger effort aimed at creating a framework for seamless and comprehensive mortgage supervision, but this framework still relies on regulators to utilize the framework to supervise and regulate the industry effectively. States have long utilized our proximity to the entities we supervise to identify emerging trends and take action when necessary. For instance, in 2009 alone, state mortgage regulators took over 9,000 actions against mortgage providers (See Exhibit B).

As the mortgage industry continued to evolve, state regulators recognized a need to create more coordinated supervision. To that end, in 2008 CSBS and AARMR established the Multi-state Mortgage Committee (MMC) to serve as the coordinating body for examination and enforcement supervision of multi-state mortgage entities (MMEs) by state mortgage regulators.

The MMC is tasked with developing examination processes that will assist in protecting consumers from mortgage fraud; ensuring the safety and soundness of MMEs; supervising and examining in an integrated, flexible and risk-focused manner while minimizing regulatory burden and expense; and fostering consistency, coordination and communication among state regulators. The MMC is made up of mortgage regulators from ten states and represents all states' mortgage supervision interests under the Nationwide Cooperative Agreement for Mortgage Supervision. I am honored to serve as a member of the MMC.

In response to the extraordinary evolution of the mortgage industry, the continuing deterioration of the real estate market, and the dramatic rise in mortgage delinquencies and foreclosures which helped fuel the financial crisis and exposed fraudulent practices, state regulators began to formalize the overhaul of their examination practices and methodologies in 2007. Regulators made an assessment that continued refinement and expansion into more sophisticated technological tools and examination techniques were necessary to enhance supervision, as well as to create more efficient regulation for the industry.

Methods of Examining

Preliminary assessment of risk by the MMC is critical to an effective examination program. Using data from the NMLS Mortgage Call Report, the MMC analyzes an MME's loan portfolio, origination practices, and financial condition to determine the safety and soundness risk of the organization and the risk it may pose to consumers. This analysis produces a risk profile which informs the MMC's prioritization process and the scope of the review.

The MMC has long held that the financial condition of MMEs is determined in large part by the degree of successful compliance with state and federal consumer protection laws and sound underwriting standards. To that end, the refinement of a broad, technologically sophisticated electronic examination initiative is a major component of the MMC examination platform. The significance and benefits of the technology are realized throughout the course of an examination, from the off-site work that occurs prior to the exam, all the way through to the compilation of the report.

This thorough examination process enables regulators to attain a 100 percent review of an MME's loan portfolio to assess its underwriting, while flagging potential compliance violations for further review. A surgical approach is then undertaken by examiners who focus on the loans identified as having potential violations. A physical review by the examiner determines whether or not the violation is in fact valid, whether consumer harm has occurred, and the degree of risk any such violation may pose to the operations of the MME. The examination also addresses issues such as depth of management; adequacy of policies and procedures; processes to identify and prevent mortgage fraud; underwriting procedures, including a determination of ability to repay; and examiner interviews with borrowers.

The automated loan review tools are a supplement to the procedures outlined in an extensive examination manual the MMC issued earlier this month. The examination approach and focus has shifted from a pure compliance check to a substantive investigation of the lending operations and financial condition of the MMEs. The culmination of the MMC's examination process is a single composite report of examination containing the findings of all participating states. Through this report, regulators and the regulated are afforded a uniform, national view of their operations and compliance performance.

This coordinated supervisory effort is intended to minimize regulatory burden and expense for the industry, and foster consistency, coordination and communication among the state regulators. Rather than subject an MME and its management to multiple state requests for electronic data uploads, the MMC is conducting these examinations under a single examiner in charge with a coordinated approach and request for information.

Combating Mortgage Fraud

Through the examinations of licensed companies and originators in their states, and through multi-state mortgage exams, state regulators identified some troubling practices and began closing mortgage companies for mortgage fraud in 2007. Exams found that both lenders and brokers were funneling a pipeline of unsustainable loans to closing, which were largely based on two premises: that potential borrowers were able to pay more on their monthly mortgage payments than they could afford; and that the products that were created allowed for a preponderance of misrepresentation on the part of both industry participants and borrowers. As the states began to receive data on rising delinquency rates, it became apparent that the methodologies the regulators were using were not adequately preventing mortgage fraud. The states quickly changed their approach and began utilizing a number of techniques in their examinations that had not previously been tried. For instance, state mortgage regulators began to attend mortgage closings, and witnessed first-hand the fabricated loan documentation that was being used to "push" loans through, even though the borrowers stated that the application figures for income were not what they had stated to the lender.

State regulators also began conducting surprise examinations in an effort to obtain documentation that was fraudulent. State regulators interview past and present employees of mortgage companies, in an effort to garner as much information on the internal processes a lender is using to process their loans. State regulators also interview current borrowers, and borrowers that have been foreclosed upon during their examinations, in addition to the traditional documentation review.

These examinations and innovative techniques produced viable documented results. The most recent example of these efforts is the prosecution and sentencing of executives at Taylor Bean and Whitaker (TBW), a national lender engaged in the underwriting and selling of mortgage loans. This successful prosecution was the direct result of a multi-state examination that began in 2008 and resulted in the exposure of vast mortgage fraud being committed at the company. A $9 million penalty heightened the case's profile, and ultimately resulted in the FHA removing authority for TBW to originate FHA loans. Just over one week ago today, the chairman and owner of TBW was sentenced to 30 years in prison and a forfeiture of $38.5 million. This is one example of many that document the effect state mortgage regulators are exerting on mortgage fraud.

LOOKING AHEAD

Across many of the industries that we regulate, we see a great deal of anxiety that reflects fears about the effect of the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act) and other regulatory actions deemed necessary to address identified weaknesses in the financial system. Coupled with uncertainty as to the structure and role of larger institutions in the economy and the future of mortgage finance, this anxiety is understandable. While financial regulatory reform was enormously challenging, the debate over mortgage finance reform will prove even more so with broad effects on consumer finance and the economy.

Appraisal Issues

As this Subcommittee knows, the regulation of appraisers includes a blend of state and federal regulatory responsibility. While the majority of state banking and mortgage regulators do not have regulatory authority over appraisers, from a safety and soundness and consumer protection standpoint, we understand that properly regulating appraisers is a critical ingredient for a healthy mortgage market. The changes made by Dodd-Frank to provide state and federal regulators with more tools in this area should benefit the overall market.

RESPA/TILA Disclosures

CSBS is supportive of providing more transparency and clarity to consumers as they deliberate what is often the most significant financial transaction of their lives. Therefore, we support the Congressional mandate imposed by the Dodd-Frank Act to streamline the disclosures currently required by the Real Estate Settlement Procedures Act (RESPA) and the Truth in Lending Act (TILA). Further, requiring fewer disclosures will reduce regulatory burden for mortgage providers and provide more efficiency for the industry. The Consumer Financial Protection Bureau recently released its initial thinking in this area. We are heartened by the generally positive reaction to their initial work and the extensive feedback provided by interested parties. The differences between RESPA and TILA have been a long-standing problem for the industry with little value to the consumer. It is possible that we are on a path towards resolution to the benefit of all.

Ability to Repay

The Dodd-Frank Act's provisions that require creditors to consider and verify a borrower's ability to repay is sound policy. Lenders should determine whether a borrower has a reasonable ability to repay, and this determination should be based on income, credit history, indebtedness, and the other relevant factors outlined in both the statute and proposed rule. Prudent lenders engage in this ability to repay analysis as a standard business practice, which reflects the economic sensibility behind this requirement. Creditors are in the business of extending loans that have a reasonable expectation of repayment, and ability to repay factors only strengthen this decision making process.

Risk Retention

As required by Dodd-Frank, the federal financial regulators have issued proposed rules implementing the Dodd-Frank requirements that securitizers retain at least 5% of the credit risk of the assets underlying asset-backed securities. In particular, the proposed rules define residential loans that will be exempt from the credit risk retention requirement, known as "qualified residential mortgages," or QRMs.

State banking and mortgage regulators support credit risk retention as a means of encouraging prudent underwriting. To achieve that goal, the federal regulators should implement a dynamic framework to monitor the performance of loans subject to credit risk retention. Additionally, the credit risk retention requirement must be implemented in a manner that enables a diverse set of institutions to be involved in originating and securitizing all loans, including QRMs. The QRM should be the least risky category of mortgage available because those securities backed by QRMs do not require securitizers to retain credit risk. At the same time, the QRM must allow for other standard mortgage products to be developed and originated, and it should not be the only mortgage available on the market.

Ultimately, the risk retention requirement represents an integral piece to a holistic regulatory effort in which we address the market and regulatory shortcomings that led to the recent economic meltdown. This requirement must be implemented in a manner that serves the law's goal of improving accountability and the alignment of incentives without creating unintended consequences for the housing market.

Loan Officer Compensation

The Federal Reserve Board of Governors (Board) introduced loan originator compensation restrictions in its proposed amendments to Regulation Z in July of 2009. The Board included prohibitions against payments based on interest rates and steering activities because disclosures alone are not always a sufficient tool to protect consumers. In a joint letter, CSBS, AARMR, and the National Association of Consumer Credit Administrators supported the loan originator compensation restriction, reasoning that

> "Deceptive loan originator compensation practices have worked to create an unfair environment for consumers. Providing financial incentives to originators to provide nontraditional mortgage loan products has led to consumers taking on excessive risks in unsuitable mortgage loans."

The Final Rule on loan originator compensation was released September 10, 2010, and became effective April 5, 2011. Though state regulators continue to support the prohibition of payments to mortgage brokers or a creditor's loan officer based on the loan's interest rate or other payment features, the rule's complexity raises significant challenges in terms of implementation. Both industry and regulators have raised many interpretive questions—

suggesting the need for guidance beyond the rule itself. This uncertainty could result in inconsistent application across the industry.

State regulators will need to determine how to examine for the regulation. In the current environment, it is very difficult to determine what is or is not a violation of the rule. At the request of the states, CSBS has coordinated a working group to develop guidance for use by state regulators. However, in absence of additional official guidance from the issuing agency, any guidelines developed by the joint state initiative will only provide a modest level of certainty for institutions as to how state examiners are evaluating compliance.

CONCLUSION

The work of state mortgage regulators over the past decade has been focused on improving and enhancing mortgage regulation to better protect the consumer and to strengthen the mortgage market itself. Key to serving these goals is ensuring that the industry is diverse and supports a variety of business models. As in other areas of financial services, state financial regulators remain concerned about policies that encourage or accelerate industry consolidation. As state regulators, we benefit from our proximity to the mortgage origination transaction and to the communities served by the mortgage industry. We hear first-hand about the regulatory burdens, and we see up close the consequences of bad actors.

The challenge for policymakers—and for the regulators who implement those policies—is to create a regulatory framework that ensures industry professionalism, industry and regulatory accountability, and the proper alignment of incentives but that also avoids unnecessary regulatory inefficiencies and burdens. For state regulators, policies and approaches that encourage regulatory collaboration and coordination and that support regulatory innovation have been vital to striking this balance.

Thank you for the opportunity to testify before you today. I look forward to answering any questions you may have.

APPENDIX

Exhibit A: Nationwide View on State-Licensed Mortgage Entities, Quarter I 2011

Exhibit B: State Mortgage Enforcement Actions From 2000 - 2009

Exhibit A

NMLS Nationwide Mortgage Licensing System & Registry

Nationwide View on State-Licensed Mortgage Entities

Quarter I 2011

Updated July 8, 2011
Conference of State Bank Supervisors
1129 20th Street, NW, 9th Floor
Washington, DC 20036-3403

Exhibit A

NMLS

A Nationwide View on State-Licensed Mortgage Entities

This report compiles data from the first quarter of 2011 concerning companies, branches, and mortgage loan originators who are state licensed or state registered through the Nationwide Mortgage Licensing System & Registry (NMLS). Unless otherwise noted, the data reflects licensing and registration information from NMLS as of March 31, 2011.

Approved Entities and Licenses in NMLS

Type	Unique Entities	Licenses
Company	14,980	28,415
Branch	15,957	24,021
Individual	100,098	182,880

NOTE: Includes companies holding a state license or a state registration through NMLS. License information includes separate licenses required for DBAs ("Other Trade Name") required in certain states and multiple licenses for different authorities (e.g. Lender and Broker) required in certain states.

Mortgage Related Business

State-licensed companies in NMLS by business activity

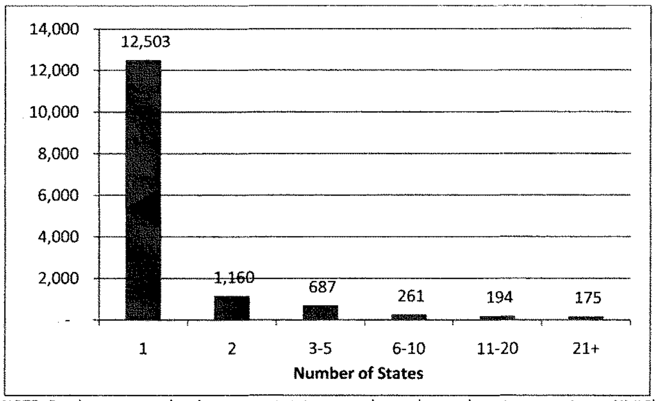
Description	Companies	% in NMLS
First mortgage loan brokering	13,298	89%
Second mortgage loan brokering	11,065	74%
First mortgage lending	3,308	22%
Second mortgage lending	2,466	16%
First mortgage servicing	1,322	9%
Second mortgage servicing	1,068	7%
Home equity loans, including lines of credit	7,038	47%
Federal Housing Administration (FHA) - Loan Correspondent	4,473	30%
Federal Housing Administration (FHA) - Direct Endorsement mortgagee	1,376	9%
Ginnie Mae approved Issuer/Servicer	340	2%
Fannie Mae approved Seller/Servicer	1,076	7%
Freddie Mac approved Seller/Servicer	940	6%
Loans guaranteed by the Veterans Administration (VA)	5,292	35%
Reverse mortgage loans	3,515	23%
High cost home loans (refer to state definitions)	1,173	8%
Other mortgage products and settlement services	1,105	7%
Credit Insurance	208	1%
Other mortgage-related business	598	4%
Engaged in non-mortgage-related business	3,269	22%

NOTE: Mortgage Related Business activity is self-reported by licensee/registrant on the "Other Business" section of their Form MU1. Licensees may be relying on different definitions in indicating their business activity. As of December 31, 2010, FHA no longer approved Loan Correspondents (See FHA Mortgagee Letter 2010-20). Answers to this section likely do not reflect this change. It is anticipated that FHA Loan Correspondent will be removed as a designation on Form MU1 in January 2012.

Exhibit A

Mortgage Companies Operating in Multiple States

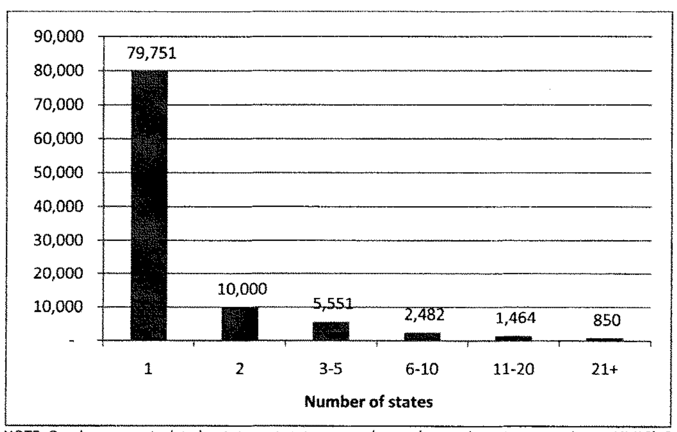
83% of companies are licensed in just one jurisdiction



NOTE: Graph represents data by state, not state agency (several states have two agencies on NMLS). For example, a company which holds a license in both California agencies is counted only once.

Mortgage Loan Originators Operating in Multiple States

80% of individual mortgage loan originators are licensed in just one jurisdiction

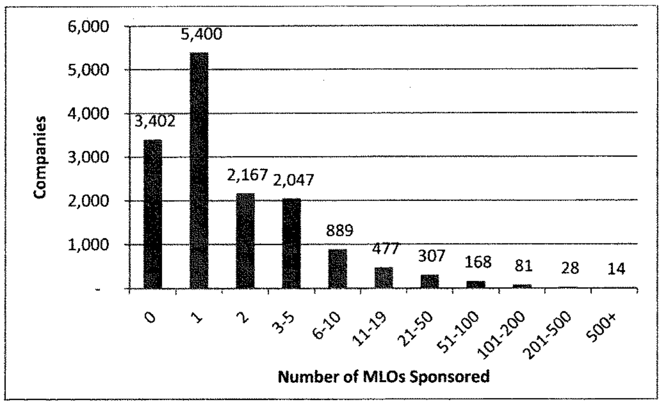


NOTE: Graph represents data by state, not state agency (several states have two agencies on NMLS). For example, a mortgage loan originator which holds a license in both California agencies is counted only once.

Exhibit A

Mortgage Loan Originators Per Mortgage Company

83% of companies employ 1-5 mortgage loan originators

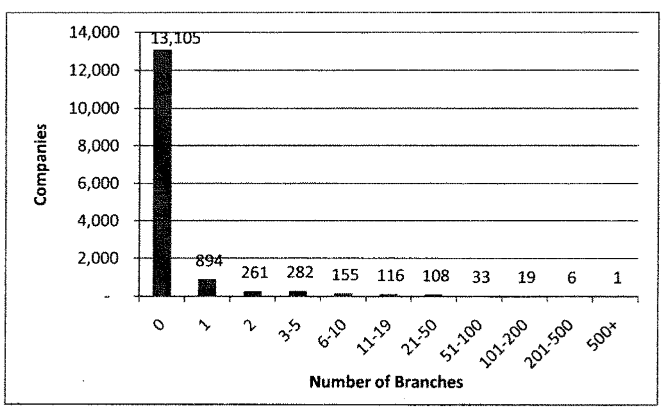


Average MLOs per Company	**5.5**
Average MLO Licenses per Company	**9.9**
Average Licenses per MLO	**1.8**

NOTE: The significant number of companies with no MLOs is due in part to the fact that some companies may hold a state license but have no individuals that must hold a mortgage loan originator license (e.g. Mortgage Servicers). The number is mostly due to the fact that some states do not require Sponsorship of MLOs by the employing mortgage company and therefore NMLS cannot provide an average.

Branches Per Company

87% of mortgage companies have only a single location

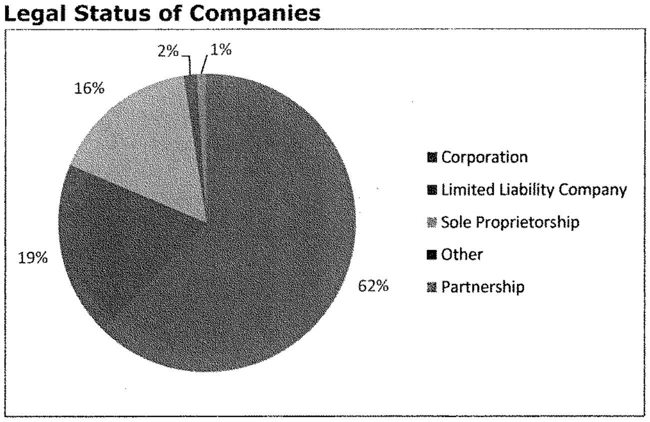


Average Branches per Company	**1.06**
Average Branch Licenses per Company	**1.58**

NOTE: Graph represents the number of Form MU3 filings per company. It is possible for a company to file two Form MU3s on the same physical location.

Exhibit A

Legal Status of Companies



Companies controlled by depository institution **287**

Exhibit A

State-Licensed/Registered Mortgage Entities
As of March 31, 2011

	Companies	Branches	Individual MLO	Average MLOs per Company	Avg Branches per Company	Companies Controlled by Deposity	
District 1							
Connecticut	623	308	4,243	6.3	0.5	30	4.8%
Delaware[2,3]	-	-	1,294	-	-	-	-
District of Columbia	326	265	1,312	3.8	0.8	34	10.4%
Maine[2,3]	-	-	1,481	-	-	-	-
Maryland	650	529	4,640	1.1	0.8	43	6.6%
Massachusetts	572	586	3,858	6.3	1.7	39	6.8%
New Hampshire	353	267	1,843	5.1	0.8	38	10.8%
New Jersey	613	792	6,740	10.3	1.3	22	3.6%
New York	1,159	930	4,843	4.0	0.8	17	1.5%
Pennsylvania	954	901	6,659	6.6	0.9	31	3.2%
Puerto Rico[1]	66	263	-	-	4.0	11	16.7%
Rhode Island	285	165	1,189	3.8	0.8	42	14.7%
Vermont	181	141	677	3.1	1.0	35	19.3%
District 2							
Illinois	678	336	5,939	7.8	0.5	39	5.8%
Indiana-DFI	261	-	2,845	10.2	-	20	7.7%
Indiana-SOS	200	28	611	2.4	0.1	3	1.5%
Iowa	330	355	1,275	3.6	1.2	33	10.0%
Kentucky[3]	351	287	2,705	0.0	0.8	14	4.0%
Michigan	628	-	3,595	8.4	-	59	9.4%
Minnesota	468	329	2,780	5.3	0.6	34	7.3%
Missouri[2,3]	-	-	2,630	-	-		-
Ohio	535	1,450	3,886	7.2	2.8	35	6.5%
Wisconsin	388	492	2,695	6.4	1.6	38	9.8%
District 3							
Alabama	416	469	2,811	6.2	1.1	19	4.6%
Arkansas	265	226	1,392	5.2	0.9	8	3.0%
Florida[1,3]	428	99	4,875	0.5	0.2	1	0.2%
Georgia	860	509	4,671	4.9	0.6	32	3.7%
Louisiana	400	433	2,483	5.6	1.1	12	3.0%
Mississippi	266	319	1,481	5.5	1.2	14	5.3%
North Carolina	546	661	5,504	8.6	1.2	17	3.1%
South Carolina-BFI	281	441	2,514	8.2	1.6	12	4.3%
South Carolina-DCA	145	101	456	2.7	0.7	1	0.7%
Tennessee	527	636	4,275	7.4	1.2	21	4.0%
Virgin Islands	15	11	26	1.5	0.7	2	13.3%
Virginia[1]	-	-	5,434	4.0	-	-	-
West Virginia	244	174	863	3.4	0.8	29	11.9%

Exhibit A

	Companies	Branches	Individual MLO	Average MLOs per Company	Avg Branches per Company	Companies Controlled by Deposity	
District 4							
Colorado[3]	715	-	4,424	3.6	-	15	2.1%
Kansas	330	347	1,747	5.0	1.1	35	10.6%
Nebraska	259	191	938	3.4	0.7	29	11.2%
New Mexico	348	348	1,749	4.8	1.0	19	5.5%
North Dakota	221	111	636	2.7	0.5	37	16.7%
Oklahoma	258	280	1,897	6.4	1.1	13	5.0%
South Dakota	155	-	473	2.9	-	10	6.5%
Texas - OCCC[2,3]	-	-	659	-	-	-	-
Texas - SML	1,444	1,445	10,557	6.8	1.0	14	1.0%
Wyoming	219	160	703	2.9	0.7	15	6.8%
District 5							
Alaska	92	77	396	3.8	0.7	5	5.4%
Arizona	685	810	4,443	5.6	1.2	13	1.9%
California - DOC	785	2,770	11,624	13.1	3.6	47	6.0%
California - DRE	4,907	749	17,695	2.8	0.2	1	0.0%
Hawaii[1]	124	55	443	3.5	0.4	4	3.2%
Idaho	345	332	1,564	4.2	1.0	11	3.2%
Montana	138	107	732	4.8	1.0	11	8.0%
Nevada	250	227	2,133	7.1	1.0	19	7.6%
Oregon	585	667	4,218	6.5	1.1	15	2.6%
Utah-DFI[2,3]	-	-	154	-	-	-	-
Utah-DRE	468	245	3,372	6.4	0.5	-	-
Washington	758	1,252	6,745	8.7	1.6	27	3.6%
Nationwide	14,980	15,957	100,098	5.5	1.1	287	1.9%

[1] Agency in the process of completing transition onto NMLS.

[2] Agency does not manage company licensing through NMLS.

[3] Agency does not require Sponsorship of MLOs by the employing company.

This report counts the number of companies, branches, and mortgage loan originators in each state, regardless of the number of licenses these entities may hold in each state. Thus, if a company holds two licenses within a state (e.g. broker and lender), the company is only counted once. The same is true for the Average MLOs per Company and Average Branches per Company. The chart is organized geographically according to the Districts established by the Conference of State Bank Supervisors (CSBS) in order to provide some regional context.

Exhibit A

State-Licensing/Registration Activity
For Period Q1 2011

	New Applications			Applications Approved			Applications Denied			Applications Withdrawn			Pending Applications			Licenses Revoked			Licenses Suspended			Licenses Surrendered		
	Company	Branch	MLO	Company	Branch	MLO	Company	Branch	MLO	Company	Branch	MLO	Company	Branch	MLO	Company	Branch	MLO	Company	Branch	MLO	Company	Branch	MLO
District 1																								
Connecticut	33	64	616	28	51	694	-	-	-	7	11	239	23	25	312	3	-	-	-	-	-	13	23	24
Delaware[1]	-	-	173	-	-	189	-	-	-	-	-	26	-	-	141	-	-	-	-	-	-	-	-	32
District of Columbia	15	31	170	31	38	174	-	-	-	1	2	10	11	17	120	-	-	-	-	-	-	5	8	5
Maine[1]	-	-	239	-	-	207	-	-	-	-	-	3	-	-	97	-	-	-	-	-	-	-	-	19
Maryland	31	72	725	20	85	702	-	-	2	9	2	306	38	43	456	-	-	-	-	-	-	11	41	22
Massachusetts	25	96	505	17	76	525	-	-	-	6	8	120	47	55	87	-	-	-	-	-	-	19	37	30
New Hampshire	8	30	251	19	35	248	-	-	-	7	10	51	16	16	139	1	-	1	-	-	-	11	18	101
New Jersey	27	82	671	41	122	631	-	-	-	-	8	73	29	59	1,518	-	-	-	-	-	-	13	79	35
New York	22	44	594	11	39	787	-	-	10	10	13	3,001	173	199	2,045	-	-	-	2	-	-	51	8	33
Pennsylvania	66	83	814	65	76	737	-	-	-	10	9	213	46	70	496	-	-	1	-	-	68	21	54	94
Puerto Rico	1	-	-	1	-	-	-	-	-	-	-	-	6	11	6	-	-	-	-	-	-	2	-	-
Rhode Island	9	26	159	9	18	109	-	-	-	3	4	14	37	42	212	-	1	-	-	-	12	12	10	5
Vermont	34	21	89	23	27	78	-	-	-	6	4	20	52	16	171	-	-	-	-	-	-	13	17	3
District 2																								
Illinois	28	30	737	14	32	956	-	-	18	2	30	15	56	28	1,108	-	-	-	-	-	-	29	2	3
Indiana-DFI	28	-	365	18	-	355	-	-	-	-	-	354	16	-	89	-	-	-	-	-	-	17	-	6
Indiana-SOS	6	7	40	5	4	34	-	-	-	-	3	12	8	3	42	-	-	-	-	-	-	7	2	17
Iowa	18	16	195	19	16	230	-	-	1	-	-	67	12	5	72	-	-	-	-	-	-	10	24	80
Kentucky	22	41	323	25	46	286	-	-	-	4	8	146	18	7	151	-	-	-	-	-	-	9	9	21
Michigan	63	-	520	44	-	708	-	-	1	19	-	205	42	-	433	-	-	-	-	-	-	17	-	12
Minnesota	43	50	525	27	85	1,125	-	-	1	3	1	16	44	17	446	-	-	-	-	-	-	6	13	-
Missouri[1]	-	-	297	-	-	261	-	-	20	-	-	97	-	-	163	-	-	-	-	-	-	-	-	8
Ohio	31	72	644	31	66	991	4	-	26	21	29	476	64	66	559	-	-	-	-	-	-	12	25	10
Wisconsin	30	125	467	51	157	471	16	-	46	2	1	73	26	12	186	-	-	-	-	-	-	14	30	63
District 3																								
Alabama	17	46	310	14	46	351	-	-	4	2	8	266	22	30	232	-	-	-	-	-	-	16	22	41
Arkansas	17	26	256	24	30	213	-	-	-	1	2	31	17	14	172	-	-	-	-	-	-	15	15	170
Florida[2]	215	160	1,279	388	98	3,854	-	-	-	29	11	23	1,692	1,097	11,003	-	-	-	-	-	-	-	-	-
Georgia	38	37	690	19	16	579	-	2	28	14	10	236	33	14	332	5	-	12	-	-	-	14	20	26
Louisiana	23	53	352	27	58	504	-	-	-	3	8	43	33	41	205	1	-	3	6	-	-	7	22	10
Mississippi	16	46	263	14	42	246	-	-	-	3	25	124	20	31	149	-	-	-	-	-	-	7	9	110
North Carolina	19	71	565	20	49	516	-	12	46	9	8	192	14	26	245	-	-	-	-	-	-	15	40	51
South Carolina-BFI[2]	35	113	344	25	162	623	-	-	-	17	62	509	37	62	624	-	-	-	-	-	-	6	5	10
South Carolina-DCA	9	8	70	5	6	46	-	-	-	1	3	19	15	5	54	-	-	-	-	-	-	3	12	9
Tennessee	18	102	473	58	103	642	-	-	16	3	-	17	32	28	304	-	-	-	-	-	-	3	29	17
Virgin Islands	1	2	6	-	2	1	-	-	-	-	-	-	1	-	7	-	-	-	-	-	-	-	-	-
Virginia[2]	35	128	765	1	96	699	-	-	3	6	7	241	779	1,002	700	-	-	-	-	-	-	-	-	13
West Virginia	22	23	169	14	23	174	-	-	-	3	-	15	20	6	39	-	-	-	-	-	-	4	5	3

Exhibit A

	New Applications			Applications Approved			Applications Denied			Applications Withdrawn			Pending Applications			Licenses Revoked			Licenses Suspended			Licenses Surrendered		
	Company	Branch	MLO	Company	Branch	MLO	Company	Branch	MLO	Company	Branch	MLO	Company	Branch	MLO	Company	Branch	MLO	Company	Branch	MLO	Company	Branch	MLO
District 4																								
Colorado[2]	190	-	536	270	-	482	-	-	-	-	-	-	79	-	1,174	-	-	-	-	-	-	-	-	-
Kansas	20	35	201	7	21	159	1	-	4	3	-	9	22	15	63	-	-	-	-	-	-	3	26	11
Nebraska	16	16	118	12	17	158	-	-	7	4	4	23	24	13	199	-	-	-	-	-	-	4	9	13
New Mexico	12	29	211	12	32	228	-	-	-	22	6	224	10	4	87	-	-	-	2	-	41	11	23	12
North Dakota	10	10	67	10	11	60	-	-	-	1	-	9	5	1	14	-	-	-	-	-	-	11	11	31
Oklahoma	18	27	164	22	40	230	-	-	-	3	6	2	22	30	309	-	-	-	-	-	-	2	3	1
South Dakota	13	-	95	13	-	99	-	-	-	1	-	14	15	-	66	-	-	-	-	-	-	4	-	5
Texas - OCCC[3]	-	-	72	-	-	96	-	-	-	-	-	45	-	-	434	-	-	-	-	-	-	-	-	-
Texas - SML	117	210	1,319	147	200	1,405	-	-	9	37	11	351	54	41	306	-	-	-	-	-	233	8	96	47
Wyoming	9	19	86	14	19	77	-	-	1	-	-	4	3	7	105	-	-	-	-	-	-	17	22	7
District 5																								
Alaska	6	10	55	7	9	54	-	-	4	1	1	14	8	3	52	-	-	-	-	-	-	2	6	1
Arizona	25	91	562	16	72	553	-	-	2	4	17	287	44	83	284	-	-	-	2	26	-	63	113	6
California - DOC	44	411	1,834	27	295	1,927	-	-	5	19	40	747	74	170	1,743	27	-	-	-	-	-	26	165	10
California - DRE	76	67	87	1,041	742	1,591	-	-	-	6	2	9	1,191	218	7,232	-	-	-	-	-	-	-	-	-
Hawaii[2,4]	42	37	201	88	44	353				9	15	22	73	55	405	-	-	-	-	-	-	-	-	-
Idaho	18	42	200	21	41	214	-	-	-	5	12	24	14	20	63	-	-	-	-	-	-	4	18	123
Montana	18	11	102	16	15	78	-	-	2	7	9	44	19	5	86	-	-	-	-	-	-	8	6	3
Nevada	15	42	217	47	35	195	-	-	-	4	7	16	28	25	166	-	-	-	-	-	-	11	12	21
Oregon	27	99	540	23	86	472	-	-	-	4	4	71	12	28	251	-	-	-	-	-	-	13	70	10
Utah-DFI[1]	-	-	51	-	-	52	-	-	8	-	-	11	-	-	30	-	-	-	-	-	-	-	-	1
Utah-DRE	34	23	217	33	35	256	-	-	5	4	-	136	15	10	158	-	-	-	-	-	3	4	12	2
Washington	52	142	745	22	139	822	-	-	1	4	56	79	89	121	227	2	2	2	1	-	-	50	227	29
Nationwide	1,767	3,026	22,341	2,956	3,557	28,507	21	14	270	339	477	9,394	5,280	3,896	36,569	39	3	19	13	26	357	623	1,398	1,416

[1] Agency does not manage company licenses through NMLS

[2] Agency was in the transition process for company licenses or registrations during the quarter

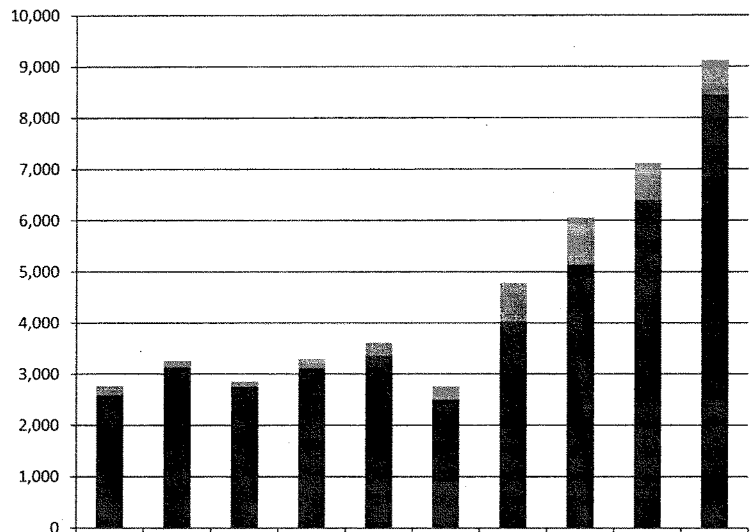
[3] Agency was in the process of completing MLO license transition during the quarter

[4] The Hawaii Division of Financial Institutions has indicated that it is not able to release the number of license applications denied.

This chart provides data on the number of license applications, application approvals, application denials, application withdrawals, license revocations, license suspensions, and license surrenders that took place between January 1, 2011 and March 31, 2011 (Quarter 1 2011) through NMLS. The chart also provides the number of licenses that were in a pending status on March 31, 2011. "License" on this chart also includes state registrations. "Application Denied" typically indicates a final denial after appeals have been exhausted, though state process and definitions may vary concerning this point.

Exhibit B

State Mortgage Enforcement Actions from 2000 - 2009



	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009
Disciplinary / Fines	180	137	93	171	249	260	761	920	719	672
Cease & Desist	1480	2002	2117	2343	2534	1596	3234	3619	3970	5957
Criminal / Revocation	1106	1127	638	782	829	904	789	1514	2424	2489

Source: LexisNexis Mortgage Asset Research Institute

Embargoed Until Delivery
2:00 p.m. EDT
July 13, 2011

STATEMENT OF

EXECUTIVE DIRECTOR JAMES R. PARK
APPRAISAL SUBCOMMITTEE
OF THE
FEDERAL FINANCIAL INSTITUTIONS EXAMINATION COUNCIL

BEFORE THE

HOUSE FINANCIAL SERVICES SUBCOMMITTEE ON
INSURANCE, HOUSING AND COMMUNITY OPPORTUNITY

HEARING ON

"MORTGAGE ORIGINATION: THE IMPACT OF
RECENT CHANGES ON HOMEOWNERS AND BUSINESSES"

JULY 13, 2011

I. Introduction

The Appraisal Subcommittee (ASC) appreciates the opportunity to provide information on behalf of the Chairman of the Federal Financial Institutions Examination Council about the Appraisal Subcommittee's mission and current activities. This statement will provide a general background and history of the ASC, including its creation in response to the savings-and-loan crisis of the 1980s, up to and including the ASC's expanded mission and authority pursuant to the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act). The statement will describe the unique system and oversight structure for real estate appraisals and appraisers that involves private, State, and Federal entities.

Additionally, the statement will discuss the responsibilities of the ASC pursuant to Title XI of the Financial Institutions Reform, Recovery, and Enforcement Act of 1989, as amended (Title XI). The Dodd-Frank Act amendments to Title XI authored by Chairman Biggert and former Congressman Kanjorski changed several provisions related to the ASC's operations, mission, and responsibilities. The statement will also address actions taken by the ASC consistent with Title XI as amended by the Dodd-Frank Act, and finally, will provide an overview of the ASC's Compliance Review process for evaluating State[1] appraiser regulatory programs' compliance with Title XI.

I. History of the ASC

Title XI of the Financial Institutions Reform, Recovery, and Enforcement Act of 1989 created the ASC as an entity within the Federal Financial Institutions Examination Council (FFIEC). The FFIEC was established pursuant to the Financial Institutions Regulatory and Interest Rate Control Act of 1978 as an interagency body empowered to set uniform principles for the examination of federally regulated financial institutions. In general, the ASC operates

[1] "State" refers to the 50 States, the District of Columbia, and five territories.

independently of the FFIEC. The mission of the ASC, pursuant to Title XI, is to promote effective appraisal standards and appraiser qualification requirements in support of the Federal and State appraisal regulatory framework governing federally related transactions, which includes any real estate-related financial transaction that a Federal financial institution's regulatory agency engages in, contracts for, or regulates, and that requires the services of an appraiser.[2]

Following the savings-and-loan crisis of the 1980s, Congress passed Title XI to address identified weaknesses regarding real property appraisals used in connection with federally related transactions. Title XI recognized the need for minimum standards for the performance of appraisals and minimum qualifications of appraisers. Prior to Title XI, appraisals for federally related transactions and the appraisers who performed them, were, for the most part, unregulated at either the Federal or State level. Poor quality appraisals were a contributing factor to the numerous bank and savings and loan failures. Therefore, Title XI sought to address this situation with an emphasis on the importance of appraisals to support safe and sound real estate lending activity of federally regulated institutions and to protect Federal financial and public policy interests in real estate transactions.

Title XI created a regulatory framework for real estate appraisals and appraisers that involves private, State, and Federal entities, including:

- The Appraisal Foundation, a private non-profit corporation, is responsible for promulgating generally accepted appraisal standards and minimum real property appraiser qualification criteria. The Foundation serves as the parent organization for two boards established to accomplish this mission: the Appraisal Standards Board (ASB) and the Appraiser Qualifications Board (AQB). These boards respectively promulgate and

[2] Title XI § 1121 (4), 12 U.S.C. 3350, as amended.

maintain the Uniform Standards of Professional Appraisal Practice (USPAP) and the Real Property Appraiser Qualification Criteria (AQB Criteria).[3]

- State appraiser regulatory agencies[4] are responsible for the certification, licensing and supervision of appraisers.
- The Federal financial institutions regulatory agencies are responsible for prescribing appropriate standards for the performance of real estate appraisals in connection with federally related transactions under the jurisdiction of each such agency.
- The ASC provides Federal monitoring, support and oversight to both the private and State entities.

The ASC Board is made up of seven members as designated by the heads of the Federal financial institutions regulatory agencies, the Department of Housing and Urban Development, and, pursuant to the Dodd-Frank Act, the Federal Housing Finance Agency (FHFA) and the Consumer Financial Protection Bureau (CFPB). FHFA appointed a representative to the ASC in November 2010. The ASC anticipates the CFPB will appoint a representative once the Bureau is established.

II. Responsibilities of the ASC Pursuant to Title XI

In response to the most recent financial crisis, Congress passed the Dodd-Frank Act, which was signed into law on July 21, 2010. The Dodd-Frank Act has added an emphasis on consumer and residential mortgage lending, recognizing that appraisals provide important information on a property, including its market value, that assists consumers in making informed borrowing decisions. With the enactment of the Dodd-Frank Act, the amendments to Title XI expanded the

[3] The AQB Criteria establishes the minimum requirements for credentialing of appraisers qualified to perform appraisals for federally related transactions, including education (for initial qualification and continuing), experience and examination.
[4] "State" refers to the 50 States, the District of Columbia, and five territories.

ASC's mission and authority and provided additional tools for the ASC in carrying out its responsibilities.

Pursuant to Title XI as amended, the ASC monitors the requirements established by States for the certification and licensing of appraisers qualified to perform appraisals in connection with federally related transactions (including a code of professional responsibility).[5] Specifically, States must adopt and/or implement all relevant AQB Criteria for the certification and licensing of appraisers.

Title XI requires the ASC to monitor both the requirements established by the Federal financial institutions regulatory agencies with respect to appraisal standards for federally related transactions under their jurisdiction, and the agencies' determinations as to which federally related transactions under their jurisdiction require the services of a State certified or licensed appraiser.

The ASC is required to maintain a National Registry of State certified and licensed appraisers who are eligible to perform appraisals in federally related transactions. Through the National Registry, State and Federal regulators, lenders, and consumers can determine whether an appraiser holds the appropriate credentials and remains in good standing with the State. The Registry became operational in 1992 and is available on the ASC website (www.asc.gov). Over the years, system enhancements have been made to the National Registry to improve public access. In March 2010, an updated National Registry system and ASC website were implemented, including automated email notification to registry subscribers on updates to National Registry information, such as credential expiration and public disciplinary actions. The updated National Registry allows authorized and properly trained personnel from each State to

[5] Title XI § 1103 (a), 12 U.S.C. 3332, as amended.

update in real time a State's own disciplinary actions taken against appraisers and National Registry submissions.

At the end of 2010, the Registry contained more than 110,000 credential entries,[6] down approximately 5 percent from the 116,000 credential entries at the end of 2009, and down approximately 9.5 percent from the peak of over 121,000 in 2007. The decrease in credential entries appears to be attributable, in part, to declining mortgage lending volume since 2007. The ASC continues to evaluate the Registry to add features that improve its value to Federal and State regulators, lenders, consumers and other users of appraisal services.

The ASC is required to transmit an annual report to Congress not later than June 15 of each year that describes its activities during the preceding year. The 2010 Annual Report has been submitted to Congress and is available on the ASC website (www.asc.gov).

The ASC is further required to monitor and review the practices, procedures, activities and organizational structure of the Appraisal Foundation. In monitoring the Foundation's Title XI-related activities, ASC staff attends AQB, ASB, and Foundation Board of Trustees meetings. ASC staff also reviews and comments on proposed and final published documents regarding the AQB Criteria and USPAP.

Pursuant to Title XI, amounts appropriated for or collected by the ASC shall be used, among other things as enumerated in Title XI, "to make grants in such amounts as it deems appropriate to the Appraisal Foundation, to help defray those costs of the Foundation relating to the activities of the Appraisal Standards and Appraiser Qualifications Boards."[7] The Appraisal Foundation submits an annual grant request to the ASC for Title XI-related activities of the ASB and AQB. The ASC provided approximately $1.28 million in grant funding to the Foundation in fiscal year

[6] "Credential entries" refers to the number of appraiser credentials, not the number of appraisers. It is not uncommon for the same appraiser to hold multiple State credentials.
[7] Title XI § 1109 (b) (4), 12 U.S.C. 3338, as amended.

2010. Between 1989 and 2010, the ASC has provided approximately $15 million in grant funds to the Appraisal Foundation. The ASC engages a public accounting firm to review the Foundation's grant-related activities and the request(s) for reimbursement.

Since 2009, the ASC has been providing the Foundation grant funds for the development, presentation, and hosting of State Investigator Training Courses. The courses, developed jointly by the Appraisal Foundation, the States, and the ASC staff, fill a void for States that would not otherwise have access to these professional development opportunities at a time when States have limited financial resources. During 2010, the course was offered in four locations across the country. Attendance at these courses included 49 of the 55 States, and over 160 State investigators, board members, attorneys and board staff participated. The grant funds paid for attendees' materials, lodging, and travel expenses for at least three individuals from each State. The course is intended to promote more effective complaint investigation and resolution by establishing training for State investigators. The training covers topics such as USPAP and proper investigative techniques, and provides resources to aid the States in their investigative processing of complaints against appraisers. Due to the positive feedback from the States, the ASC approved funding for additional investigator courses for 2011.

The Dodd-Frank Act contains several provisions related to the ASC's operations, mission, and responsibilities. The most significant provisions address:

- Addition of the FHFA and CFPB as Federal agencies with representation on the Appraisal Subcommittee;
- Authority to monitor States' regulation of Appraisal Management Companies (AMCs);
- Rulemaking authority with regard to (1) temporary practice, (2) National Registry, (3) information sharing, and (4) enforcement;

- Authority to provide grants to the State programs;
- Requirement for States to have a policy for issuing a reciprocal certification or license to an appraiser from another State under certain conditions;
- Requirement for States with an appraiser license level category to adopt and implement the minimum qualification criteria issued by the AQB;
- Minimum qualification requirements established by a State for individuals in the position of "Trainee Appraiser" and "Supervisory Appraiser;" and
- Establishment of a National Appraisal Complaint Hotline.

As a result of these new Federal statutory mandates, States will need to revise their programs and, in some States, may need to adopt legislation or regulations to implement changes to their programs. Actions already taken by the ASC pursuant to the requirements of the Dodd-Frank Act include:

- *ASC Meetings:* In October 2010, the ASC approved amendments to its Rules of Operation to implement formal open meeting requirements in the legislation. Through the ASC's website and publication in the *Federal Register*, the public receives advance notice of the ASC's monthly board meetings and may attend the open session with advance notification.
- *ASC Membership:* In November 2010, the FHFA designated a representative to the ASC. The FHFA staff attended ASC meetings as observers in advance of formally designating a representative. The CFPB staff recently began attending ASC meetings in advance of CFPB formally designating a representative.
- *Modification to the ASC National Registry Fee:* To be listed on the National Registry, appraisers are required to pay an annual registry fee to States which remit the funds to the

ASC. On October 13, 2010, the ASC approved an increase in the annual National Registry fee from $25 to $40 to support its activities, including additional authority under the Dodd-Frank Act.[8] The fee increase takes effect January 1, 2012. This is the first increase in the National Registry fee since Title XI established the fee in 1989.

- *National Appraisal Complaint Hotline:* The Dodd-Frank Act required, within six months of its enactment, the ASC to determine whether a national appraisal complaint hotline existed to receive complaints of noncompliance with appraisal independence standards and USPAP. At its January 12, 2011 open meeting, the ASC determined that an appraisal complaint hotline as prescribed in the Dodd-Frank Act was not currently in operation. Consistent with the Act's mandate, the ASC is now studying the establishment and operation of a national appraisal complaint hotline.
- *GAO Study:* The Dodd-Frank Act required the GAO to conduct a study on the ASC. That study is currently underway and scheduled to be completed by the end of 2011.

The Dodd-Frank Act also requires the ASC to undertake several other reforms, which the ASC has not yet fully implemented. For example, the ASC must monitor the requirements established by States for the registration and supervision of AMCs[9] and maintain a National Registry of AMCs, which is dependent upon the establishment of AMC registration framework requirements by the Federal financial institutions regulatory agencies, FHFA and the CFPB. The

---

[8] See 75 *Federal Register* 65629 (October 26, 2010).

[9] Pursuant to Title XI § 1121 (11), as amended by the Dodd-Frank Act, the term "appraisal management company" means, in connection with valuing properties collateralizing mortgage loans or mortgages incorporated into a securitization, any external third party authorized either by a creditor of a consumer credit transaction secured by a consumer's principal dwelling or by an underwriter of or other principal in the secondary mortgage markets, that oversees a network or panel of more than 15 certified or licensed appraisers in a State or 25 or more nationally within a given year—

(A) to recruit, select, and retain appraisers;
(B) to contract with licensed and certified appraisers to perform appraisal assignments;
(C) to manage the process of having an appraisal performed, including providing administrative duties such as receiving appraisal orders and appraisal reports, submitting completed appraisal reports to creditors and underwriters, collecting fees from creditors and underwriters for services provided, and reimbursing appraisers for services performed; or
(D) to review and verify the work of appraisers.

commencement date for the AMC Registry and the annual AMC registry fees will be dependent upon the adoption of the Federal regulations and establishment of the State's AMC registration framework.

Overview of State Compliance Review Process

A key part of the ASC's mission is to monitor and assess State appraiser regulatory programs. State programs are assessed every two years, through an on-site Compliance Review process, for compliance with Title XI. Compliance Reviews are scheduled to coincide with a meeting of a State program's decision-making body whenever possible, and are conducted over a two- to four-day period. ASC staff assess the State programs for compliance with Title XI, ASC Policy Statements,[10] and AQB Criteria. For example, ASC staff will assess whether States' appraiser qualification criteria meet the AQB Criteria, and whether States are taking disciplinary actions against appraisers in a responsible and timely manner so that incompetent and unqualified appraisers are not allowed to conduct appraisals for federally related transactions. The ASC's Compliance Review of the State programs focuses on three key components of Title XI: (1) implementation and enforcement of USPAP and the AQB Criteria; (2) adequacy of the State's statutory or regulatory authority, funding and staffing to successfully carry out Title XI-related functions; and (3) consistency with Title XI in the decisions of the State programs.

Over the past three years, the ASC has taken steps to increase and improve communications with the States. Last year marked the second full year the ASC conducted State reviews under the revised ASC Compliance Review process, and with positive results. During the 2009-2010 review cycle, 41 percent of the States were found in substantial compliance with Title XI as compared to 16 percent during the 2007-2008 review cycle. The new process provides a State

[10] The ASC periodically issues Policy Statements to assist the States in understanding the ASC's expectations for State programs. The Policy Statements reflect the general framework that the ASC uses in the Compliance Review process. Any revisions to the Policy Statements would be considered in light of the ASC's new rulemaking authority as established by the Dodd-Frank Act.

with an opportunity to review the ASC staff's Preliminary Findings, ask for clarifications and provide their response to the ASC prior to a final determination of compliance. Once ASC staff completes their Preliminary Findings, which are communicated in an ASC staff report to a State, the State is given 60 days to respond. The ASC staff then considers the State's response(s) and makes formal recommendations to the ASC Board members for final disposition. The ASC Board members consider the ASC staff report and recommendations along with responses from the State before rendering a decision.

The ASC Board members issue a final Compliance Review Report and letter to the State with a determination regarding the State's compliance with Title XI. State programs are found to be either: (1) in substantial compliance; (2) not in substantial compliance; or (3) not in compliance.

The general areas of non-compliance with Title XI and the number of States experiencing those problems are presented in the 2010 Annual Report available on the ASC website (www.asc.gov). Timeliness of the investigation and resolution of complaints against appraisers continues to be the most common area of non-compliance for the States.

In 2010, the ASC staff conducted 26 Compliance Reviews and eight Follow-up Reviews. In addition, ASC staff conducted six State Priority Contact Reviews which are scheduled on an as-needed basis. These Priority Contacts provide ASC staff the opportunity to visit with a State that may pose a relatively high risk to the appraisal regulatory system, such as a State with a large population of appraisers, a State with major changes to the program leadership, or a State with past compliance concerns.

As reported in the ASC 2010 Annual Report, eight States collectively represented over 50 percent of the appraiser credentials on the National Registry and, therefore, are reviewed on an annual basis. This included California, Colorado, Florida, Georgia, Illinois, New York, Texas, and Virginia.

The following table, based on information from the ASC 2010 Annual Report, recaps the results of the 2008, 2009, and 2010 Compliance Reviews organized by the requirements and areas of guidance considered by the ASC in the review of a State's appraisal regulatory program. As disclosed in the ASC 2010 Annual Report, States face significant challenges given the current financial environment, which has placed a strain on several States' resources for their appraiser regulatory programs.

Areas of Non-Compliance			
Requirement/Guidance Areas	26 States Reviewed for Compliance in 2010	32 States Reviewed for Compliance in 2009	26 States Reviewed for Compliance in 2008
	2010 26 States Reviewed	2009 32 States Reviewed	2008 26 States Reviewed
Statutes, Regulations, Policies and Procedures:	4	7	15
Temporary Practice:	1	0	8
National Registry:	1	1	4
Application Process:	9	19	8
Reciprocity:	0	0	0
Education:	0	0	0
Enforcement:	19	15	16
State Compliance Status			
	2010 26 States Reviewed	2009 32 States Reviewed	2008 26 States Reviewed
In Substantial Compliance	10	14	5
Not in Substantial Compliance	16	18	20
Not in Compliance	0	0	1

Title XI authorizes the ASC to take action against a State in the case of non-compliance, which historically was limited to an order of non-recognition. Such an order would effectively mean that federally regulated financial institutions would be unable to conduct real estate lending in a non-compliant State as institutions would be unable to employ the State's appraisers for appraisals in federally related transactions. Pursuant to the Dodd-Frank Act, the ASC now has new rulemaking and additional sanctioning authority. With regard to any future ASC rulemaking, the Dodd-Frank Act directs the ASC to establish an advisory committee of industry participants, including appraisers, lenders, consumer advocates, real estate agents, and government agencies, and hold meetings as necessary to support the development of such regulations.

Conclusion

In conclusion, the Dodd-Frank Act made significant amendments to Title XI that will take several years to fully implement. Given the significant new responsibility and authority given to the ASC, staffing and other resources are being carefully analyzed and monitored to ensure the agency has the proper resources to fulfill its Title XI requirements. As stated in the 2010 ASC Annual Report, the ASC has indicated its dedication to carrying out its new and existing Title XI mandates transparently and efficiently.

Testimony of Teresa B. Payne

Associate Deputy Assistant Secretary for Regulatory Affairs

U.S. Department of Housing and Urban Development

Subcommittee on Insurance and Housing

"Mortgage Origination:

The Impact of Recent Changes on Homeowners and Businesses"

July 13, 2011

Thank you, Chairman Biggert, Ranking Member Gutierrez, and members of the Subcommittee for this opportunity to bring you up to date on the status of the Real Estate Settlement Procedures Act ("RESPA") and the transition of its statutory authority from the Department of Housing and Urban Development to the Consumer Financial Protection Bureau.

Before discussing how RESPA will transition from HUD to the CFPB, both in terms of statutory authority and personnel, it is perhaps best to explain first the status of RESPA at HUD currently, and then to go into detail regarding the transition moving forward.

The Office of RESPA and Interstate Land Sales ("ILS").

The Office of RESPA and ILS currently has 21 staff members including the Director, the Deputy Director, four Compliance Team Supervisors, eleven RESPA Compliance Specialists, three ILS Compliance Specialists, and one Administrative Assistant. It is housed at HUD headquarters here in Washington, DC, without any satellite offices.

During 2010 and 2011, the RESPA complaint caseload has been extremely heavy. More than 1,500 cases were opened in the last 18 months. Moreover, the Office's increased caseload led to increased enforcement activity, which has in turn involved greater coordination with state regulators to share information about real estate settlement practices and regulatory compliance. Monthly collaborative telephone calls among RESPA staff and state regulators from numerous state offices are routinely attended by representatives of more than 25 states. The RESPA Office has also been working more closely with the Department of Justice and HUD's Office of Inspector General in investigation and enforcement actions.

As you are aware, in November 2008, the Department issued a new RESPA regulation that established a standard, required Good Faith Estimate form and process, in coordination with a revised and expanded HUD-1 Settlement Statement, for more clarity, transparency and better understanding by consumers in the real estate settlement process. To be in compliance with RESPA, and help assure fair prices for consumers, actual costs at closing must fall within established tolerance ranges.

The new disclosures were implemented on January 1, 2010. Before then, beginning in December 2008 and continuing today, the RESPA Office established a compliance guidance regimen to educate industry participants, state and federal regulators, housing counselors and consumers.

A few of the educational tools utilized by the Office include:

- Speaking to over 175 organizations in person, by phone and via the web;
- These speaking engagements have reached more than 25,000 people directly;
- To further assist industry and regulators, the Office periodically publishes on its website the "RESPA Roundup," which is unofficial guidance addressing relevant compliance questions. In addition, this guidance is distributed by email to over 4,500 recipients that are on the Office's direct distribution list; and
- Similarly, the Office published on its website 300 Frequently Asked Questions and Answers, which are also unofficial guidance, on the new RESPA rule. These FAQs have been downloaded tens of thousands of times and have been a major guide for industry.

In addition to all of the guidance described above, in order to reach out directly to better inform consumers, the RESPA Office produced and released three consumer education videos:

- ➢ *Shopping for a Home;*
- ➢ *Shopping for a Loan;* and
- ➢ *Closing the Deal.*

These videos have been viewed thousands of times and assist consumers in the home buying and mortgage loan process. Additionally, a new settlement cost booklet that must be delivered to consumers within three days of loan application was also published.

RESPA Office staff members answered more that 15,000 e-mails and handled more than 4,700 phone inquiries in 2010 and 2011. As you can imagine in a period of extensive implementation, the vast majority of these inquiries were received from industry stakeholders, and the inquiries were responded to quickly and informatively.

Although it has only been six months since completion of the 2010 implementation year, some tangible results are being seen. Prospective borrowers are receiving more accurate Good Faith Estimates and costs at closing are being held within tolerance ranges. Several commenters noted that the new GFE form is holding lenders accountable for low-balling and bait-and-switch, which have made estimates closer to the actual closing costs. In some cases where tolerances were exceeded, borrowers received refunds for the overage from loan originators. In addition, RESPA staff has assisted borrowers in saving hundreds or thousands of dollars through tolerance violation cures and loan term corrections per loan. In some instances this has amounted to in excess of $100,000.

Specific Guidance Documents Published during 2010-2011.

Several interpretive rules and policy pieces have been published during the last 18 months. I would like to discuss several of these in more detail.

- The Home Warranty Interpretive Rule.

  Home warranties have been expressly covered as a settlement service under HUD's regulations since 1992, and HUD staff has subsequently provided informal guidance on fees paid to real estate agents for placement of home warranties.

  In February 2008, an unofficial staff interpretation letter responding to an inquiry explained the framework for applying HUD's RESPA regulations to compensation of real estate agents for providing home warranty services. This letter was widely circulated among industry and led to requests for more-formal and comprehensive guidance.

  In June 2010, HUD issued an interpretive rule regarding compensation arrangements for real estate agents in connection with the sale of home warranties to home sellers and buyers. Although public comment is not required for interpretive rules, HUD also invited public comment on the clarity and scope of the interpretive rule. In December 2010, the Department published additional clarifying guidance in this area.

  The Home Warranty interpretive rule and additional guidance interpret Section 8 of RESPA and HUD's regulations that implement referral and kickback prohibitions as these apply to the compensation to real estate brokers and agents from home warranty companies. Briefly, the guidance states that, in order for such compensation to be acceptable:

(1) A real estate broker or agent must perform actual and necessary services that are distinct from their primary services and for which there are not duplicative fees; and

(2) The compensation must be reasonably related to the value of the services actually performed.

The interpretive rule and subsequent response to public comments also provide examples of services that real estate agents could perform for which they might be legitimately compensated, depending on the facts of the situation. Some of these examples had been suggested by the industry in submissions to HUD.

The examples include conducting actual inspections of the items to be covered by the warranty to identify preexisting conditions that could affect home warranty coverage, recording serial numbers of the items to be covered, documenting the condition of the covered items by taking pictures and reporting to the HWC regarding inspections.

While this remains an issue on which there are concerns among some industry participants, HUD believes strongly that the interpretive rule and guidance clarify important consumer protections.

Additionally, you have asked HUD to review and comment on the recently proposed legislation entitled the "RESPA Home Warranty Clarification Act of 2011." While the Administration has not taken a formal position on the bill, HUD has concerns that the proposed legislation could limit consumer protection in the context of home warranties and lead to higher closing costs for consumers through referral fees. Such a result would be in contrast to the purposes of the statute and would erode the statute's consumer protections.

HUD recommends — prior to enacting legislation — that a study be conducted by appropriate regulatory agencies about the quality of home warranties, including a review of their use by homeowners and homebuyers, business practices around their sale, representations made to consumers at the time the home warranty is marketed, and what is included or excluded in home warranty contracts.

- Guidance was also issued through a Secretarial exemption, which had been requested by over 125 nonprofit organizations with "soft seconds." Subordinate loans provided by assistance programs for low- and moderate-income persons were exempted from RESPA's Good Faith Estimate and the HUD-1 Settlement Statement requirements.

- The RESPA Office also drafted unofficial guidance, which was posted in a "RESPA Roundup," clarifying how the Federal Reserve Board's Mortgage Loan Origination Compensation Rule that was going to take effect on April 1, 2011, would be consistent with the RESPA disclosure requirements.

The guidance addressed:

(1) Mortgage broker transactions where the broker is compensated indirectly from the lender by means other than an amount computed based on the interest rate, such as by a flat fee or an amount that is based on any other computation;

(2) No cost transactions where the credit for the interest rate chosen covers third party settlement charges;

(3) Using a credit/charge calculation prior to completing portions of the Good Faith Estimate; and

(4) Payments by lenders to borrowers to correct tolerance violations in mortgage broker originated transactions.

Overall, the guidance helped consumers and industry to have a better understanding of the interaction between RESPA and the Board's rule.

- In November 2010, the Department solicited general information on warehouse lending and other financing mechanisms used to fund federally related mortgage loans, including how those mechanisms have evolved in recent years. Under HUD's RESPA regulations, warehouse lending arrangements are generally secondary market transactions that are not covered by RESPA. In early 2011, after reviewing comments received, the Department released two letters explaining that the same analysis that HUD would use to determine if a traditional warehouse lending arrangement was a secondary market transaction would be used to determine the application of RESPA to other arrangements with similar characteristics, such as repurchase agreements.

Transition from HUD to the CFPB.

Now that I have explained some of the recent regulatory actions and proposed legislation regarding RESPA, I would like to turn to the question of how the statutory authority and RESPA-related functions and personnel will transition over to the CFPB. I would note at the outset that I am still an employee of HUD and will not be an employee of CFPB until July 31, 2011. Therefore, I am not authorized to speak on behalf of the CFPB. Notwithstanding that restriction, however, there are certain aspects of the transition that are commonly known.

First, pursuant to the requirements of the Wall Street Reform and Consumer Protection Act ("Dodd-Frank"), on July 21, 2011 – next week – the statutory authority for RESPA will formally transfer from HUD to the Consumer Financial Protection Bureau. The transition of personnel currently has 37 HUD staff slated to become CFPB employees by July 31, 2011. The reduction in staff had been taken into consideration at the time of preparing the FY 2012 budget request.

Second, I would note that under the terms of Dodd-Frank, RESPA is merely one of 18 statutory authorities that will transfer to the CFPB. This point is significant. Although the Office of RESPA at HUD currently handles all aspects of the statute—consumer in-take, industry questions, investigations and enforcement actions, FOIA requests and Congressional inquiries—these functions and related HUD personnel will be dispersed throughout the CFPB. Specifically, HUD staff members will be placed in CFPB's Office of Consumer Response, the Office of Enforcement, Rulemaking, the Office of General Counsel, Consumer Education and External Affairs. Thus, there will be a shift from a subject matter-based approach to RESPA at HUD, to a more functionally defined approach to RESPA at the CFPB.

Additionally, each function may require addressing a combination of statutes. For instance, mortgage loans may require the simultaneous understanding of RESPA, Truth in Lending Act (TILA), and the Fair Credit Reporting Act (FCRA) for a rulemaking, an enforcement action or simply an inquiry from a stakeholder.

Finally, as you may be aware, the CFPB has begun undertaking another Dodd-Frank statutory requirement – to create a new model disclosure form that combines RESPA Good Faith Estimate information and TILA loan disclosure information. This model form must be proposed within one year of the statutory transfer date – July 21, 2012. Throughout 2009 and 2010, HUD staff had been consulting first with Federal Reserve staff and during 2011 with CFPB staff in developing a combined RESPA-TILA disclosure. Prototypes of these disclosures were published in May 2011 on the CFPB website for comment.

Thank you for this opportunity to appear before you and I look forward to answering any questions that you may have.

"Mortgage Origination: The Impact of Recent Changes on Homeowners and Businesses."

Before the U.S. House of Representatives Committee on Financial Services
Insurance, Housing and Community Opportunity Subcommittee

July 13, 2011

Testimony provided by:
Ira Rheingold
Executive Director
National Association of Consumer Advocates
1730 Rhode Island Ave, NW
Washington, D.C. 20036

Chairperson Biggert, Ranking Member Gutierrez, and members of the Subcommittee, thank you for inviting me to testify before you today on the subject of "Mortgage Origination: The Impact of Recent Changes on Homeowners and Businesses."

My name is Ira Rheingold, and I have been a public interest attorney for my entire adult career. I have worked in some of our nation's poorest urban and rural communities and I've witnessed the incredible resilience and optimism that mark the great strength of our nation's people. I have also seen the incredible fear and despair experienced by American families and their communities as they faced and continue to bear the brunt of the worst housing and economic crisis of our lifetime.

In the mid – 1990's through 2001, I lived and worked in Chicago, where I ran the Legal Assistance Foundation's Homeownership Preservation Project. During those years, I watched (and worked against) the unfair and deceptive practices of many actors in the mortgage industry, that slowly, but inexorably stripped away the wealth of that city's low and moderate income minority communities. Today, I am the Executive Director of the National Association of Consumer Advocates (NACA), an organization of attorneys and other advocates who represent those very same consumers and communities all across this country. At NACA, I also manage the Institute for Foreclosure Legal Assistance, a project that provides funding and training to non-profit legal organizations that help homeowners negotiate alternatives to foreclosure. In my current roles, I speak to and assist our nation's consumer advocates who, on a daily basis, meet with and represent the consumers who have been victimized by bad mortgage lending and servicing practices and see the very real-life consequences of what an out of control mortgage lending marketplace did to our communities and our nation's economy

Introduction

Before I address recent changes to rules effecting mortgage origination, I think it's essential to put any recent reforms into the context of what the mortgage making process looked like until its bubble burst and shattered our economy. The mortgage market of the late 1990s and early 2000s, in no way resembled what most of us thought we understood about buying a home or getting a loan. I have talked to thousands of consumers, who believed (or were led to believe) that the mortgage entity that originated their loan, would only profit when they timely made their monthly mortgage payment. While this may have been the case when our parents or even our grandparents bought their homes, this was not true for most of the past two decades. Instead, because of the growth of securitization as the tool to fund both prime and subprime mortgages, with all its confusing layers, multiple actors and often perverse incentives, the nature of the consumer- mortgage originator relationship, unbeknownst to the consumer, has fundamentally changed. These changed relationships and backwards incentives led us to housing market mess that we are still trying to clean up.

Securitization and the Consumer

For my purpose today, I'm going to keep this very simple. At its most basic level, securitization is a process, which involves the pooling and repackaging of cash-flow producing financial assets into securities that are then sold to investors. As securitization grew to be the dominant way that mortgage loans were funded, the role and purpose of mortgage originators (and all the other actors in the mortgage market) fundamentally changed.

For the most part, the notion of lenders keeping a loan on their books for the duration of the loan was no longer the reality. With securitization, lenders/mortgage originators generated profits, not from the payments they would receive from the borrowers over the length of the loans, but instead from the fees they collect from selling the loans to investment banks.[1] Mortgage originators essentially became manufacturers of a commodity, the American mortgage borrower. Unfortunately, most homeowners did not and don't understand their role in this transaction. This commodity was then sold to the capital markets, which in turn, chopped, spindled and mutilated this new commodity into something that could be purchased by investors from around the world.

While advocates of securitization argued that the process produced additional capital and greater access to homeownership for some consumers, they failed to recognize the fundamental shift and potential dangers it created by fundamentally changing the traditional borrower-lender relationship in the consumer marketplace. No longer was the borrower's best interest (or even their ability to repay the loan) part of the mortgage transaction calculation. Instead, the real transaction was between the mortgage originator and the investment bank, which not only set the standards for the borrower/product they wanted to buy (and then turn around and sell), but also provided the money for the originators' loans.

Under these set of circumstances, what American consumers needed was the vigorous enforcement of existing consumer protections as well a new set of consumer protections to correspond with the very different mortgage world that had now been created. Unfortunately, what the federal government gave us was the exact opposite, not only diminishing its regulation and enforcement of this market, but providing interference and protection (under the guise of preemption) for mortgage market players when states, recognizing the fundamental flaws in the system, attempted to protect their own citizens.

The mortgage market, unfairness, deception and the consumer

Understanding what mortgage originators (and all of the actors in the process) were attempting to do, i.e. creating commodities to sell, when they made a loan to a consumer helps us understand all the unfair and deceptive practices that recently flourished in the mortgage marketplace. A clear misalignment of incentives lay at the heart of the recent mortgage meltdown. [2] In the past,

---

[1] Raymond Brescia. "Leverage: State Enforcement Actions in the Wake of the Robo-Sign Scandal," Albany Law School Working Paper Series No. 38, 5, December 16. 2010.

[2] For a much longer discussion of the roots of today's crisis, see Testimony of Eric Stein, Center for Responsible Lending, before the Senate Committee on Banking (Oct. 16, 2008), *available at* http://www.responsiblelending.org/pdfs/senate-testimony-10-16-08-hearing-stein-final.pdf.

the interests of borrowers and lenders were perfectly aligned: if the borrower did not pay the mortgage, the lender did not make money. But the proliferation of independent brokers and the growth of the secondary market upset this alignment of interests between lender and borrower by creating a system where each actor was compensated early in the loan transaction, often within the first month of the loan term, thereby reducing or even eliminating the incentive to worry about how the borrower would fare later on.[3]

I'd like to talk about some of those practices now, and explain why unless all these issues are sufficiently addressed, we will not be able to rebuild a fair, responsible and functional mortgage origination marketplace.

A. The Predatory Pitch

As the demand for product to sell to Wall Street investment banks grew (ultimately exponentially), the pitch to vulnerable homeowners (and prospective homeowners) became more targeted and more personal. Armed with financial and personal data and carefully conducted research, mortgage brokers and lenders used TV and radio advertising, mailings, telephone calls, and even home visits to reel in consumers who otherwise had no real reason to get a new home mortgage. With promises too good to be true ("refinance your home, fix your roof and lower your monthly payment") consumers were later *bait and switched* to loans far more expensive than they thought they were promised. Because the mortgage "originators" received their full compensation when they manufactured the "product/borrower" to sell onward and upward, there was little concern whether the loan was sustainable. As many of us knew, and most of us have now learned, many of those loans were completely unsustainable.

B. The Over-Inflated Appraisal

In a rational world, a consumer would not want to pay (or borrow) more for a home than what it was worth. In the securitization created "bizarro" mortgage world, an over-inflated house made perfect sense to the parties involved in the transaction (except for the unsuspecting consumer and the ultimate investors left holding the bag). Let's look at the parties to the transaction. We have the mortgage originator (the broker or the lender or sometimes both) whose incentive was quite obvious. Simply put, the greater the house price, the larger the loan, the greater the fee they received from the transaction. (The same can be said for the investment bank). Sometimes the incentives are a little more complicated. Take for instance a homeowner

[3] For additional background on the development of the market that led to the mortgage crisis see Testimony of Julia Gordon before the House Committee on Financial Services, Subcommittee on Financial Institutions and Consumer Credit (March 11, 2009) available at: http://www.responsiblelending.org/mortgage-lending/policy-legislation/congress/gordon-testimony-3-11-09-final.pdf

whose existing mortgage is already 100% of the actual value of the home. If the real house value was used, no loan could be made, no product could be created. So the house value was increased to meet the loan purchasing parameters (the underwriting guidelines) set by the investment bank and the loan was made and everyone was happy (including the "unknowing" investment bank who had another product to slice and dice and sell to someone else).

As for the appraiser who creates the fraudulent value for the home, we've seen time and again why they went along with this fraud. Simply, if they actually wanted to stay in business and continuing doing appraisals, they created the value the mortgage originator wanted.

What we had left (by the millions), were consumers who had a mortgage that was worth far more than the real value of their home.

C. Yield Spread Premiums and Prepayment Penalties

Unfortunately (for me), I have been around long enough to hear multiple and ever-shifting explanations as to why yield-spread premiums ("YSPs") were an acceptable practice and why they work for consumers. I can safely state, that none of those arguments are true in the mortgage marketplace that actually exists in our country. I do however, fully understand why they work for every mortgage market actor except, again – of course - for the consumer.

When a mortgage broker is involved in the origination of a loan, the broker's fee is one of the larger "upfront" costs. Basically the yield spread premium is a type of mortgage broker fee that includes increasing the interest rate of the loan. Essentially, mortgage brokers get paid more if they produce mortgages with an interest rate higher than what a borrower qualifies for. Yield spread premiums incentivized mortgage brokers to push loans with unnecessarily higher costs and risky loan terms. The idea is that a borrower is supposed to be able to reduce or eliminate the upfront origination costs in exchange for paying this higher interest rate.[4] However, this rarely occurs. Often borrowers pay more not only on high interest rates, but also for broker's services and other closing costs.[5] When compared to similar loans, mortgage brokers receive about $800 to $900 more in additional fees for YSP loans than those without.[6] Unless a

---

[4] *See* Center for Responsible Lending and National Consumer Law Center Amicus Curiae Brief in Support of Defendant Federal Reserve Board's Opposition to Plaintiff's Motions for Temporary Restraining Order and Preliminary Injunction, *National Association of Mortgage Brokers and National Association of Independent Housing Professionals, Inc., v. Board of Governors of the Federal Reserve System*, No. 1:11-cv-00506-BAH and No. 1:11-CV-00489-BAH, 7-8, (D.D.C. March 23, 2011) citing Howell E. Jackson and Laurie Burlingame, *Kickbacks or Compensation: The Case of Yield Spread Premiums*, 12 Stan. J. L. Bus & Fin. 289, 338 (2007).

[5] See Center for Responsible Lending and National Consumer Law Center Amicus Curiae brief citing e.g. Susan E. Woodward, U.S. Dep't of Housing and Urban Dev., Office of Pol'y Dev. And Research, *A Study of Closing Costs on FHA Mortgages*, (2008).

[6] Center for Responsible Lending and National Consumer Law Center Amicus Curiae brief citing Jackson & Burlingame, Kickbacks of Compensation, 12 Stan. J. L. Bus & Fin. at 323.

mortgage broker actual lives up too their off-stated (but never written) commitment to serve in the best interest of their consumer client, their incentive – a bigger paycheck - to produce a loan with a YSP is clear. Same with the mortgage lender and investment bank, who now have a loan with a bigger interest rate to sell.

To make matters worse, almost any loan with a YSP is sure to have a prepayment penalty. In plain English, a prepayment penalty is a charge to a borrower who repays their loan "too soon," typically during the first few years of the loan's existence. What makes this product so cynical, and so closely intertwined with a YSP, is that the very existence of the YSP means that the consumer has an interest rate that is higher than they actually qualify for. Therefore, if the consumer acts rationally and shops for a lower interest and enters into a new mortgage, they will be punished with a steep prepayment penalty.

In all my years talking, interviewing, and representing consumers, I never met one consumer who actually understood that they were charged a YSP or that the YSP led to a higher interest rate than they were otherwise qualified for. I simply can't imagine how this practice was not deceptive or just plain unfair. Abuse of this practice increased the likelihood that loan originators will improperly steer consumers into risky and expensive loans. It was harmful not only to prospective homeowners but also to the soundness of the housing market.

D. The Disappearance of Escrow Accounts

Because the borrower has become the product to be created and sold, mortgage originators became experts at getting borrowers to take out loans that make little or no economic sense. A classic and pervasive practice in the all too recent mortgage market was the "promise" that a new loan would allow the borrower to pay a lower monthly mortgage payment. What the borrower was not told was that their new payment did not include their taxes and insurance (for escrow), so that their lower payment really was just a mathematical fiction (otherwise known as a lie).

E. Reckless Underwriting and the Rise of Community Endangering Loan Products

In place of an efficient market that provides real consumer choice and rewards consumers for smart credit decisions and rational aspirations, what we saw was a mortgage market that has recklessly created and sold risky mortgage products that excessively benefited all of the market players at the expense of the American consumer and our nation's communities. In a rational marketplace these loans made no sense. Looking at them however through the lens of a fundamentally flawed and previously unregulated mortgage marketplace, they unfortunately made perfect sense (at least at the time they were made).

Simply put, in order to meet the demand of voracious Wall Street investors, originators ignored basic, common-sense underwriting principles to boost their loan volume with new "exotic" mortgage products. Instead of the traditional 30-year fixed rate mortgage, no-doc or "stated-income" loans were created so loan originators could make more money (it was less work and they could charge borrowers a higher interest rate) and they fed the beast that wanted high-risk products that would produce a higher return for investors. Underwriting adjustable rate mortgages only at the initial interest rate, without considering how homeowners would be able to pay their loans once the payment adjusted upward, was also quite profitable for mortgage originators and the investment banks that were fed by them. These fundamentally unsustainable loan products, in all their derivations (including 2-28s and option ARMs) were destined for failure and failed they have and we still are living with the consequences.

In response to this crisis, Congress finally and belatedly took action, by passing the historic "Dodd–Frank Wall Street Reform and Consumer Protection Act" (Dodd-Frank). While I'm happy to and will address some of the important mortgage origination reforms created by this necessary and important law, the question before our panel today seems extremely premature as to the impact of both Dodd-Frank and reforms made or being contemplated by bank regulators. Simply, we really won't know how successful the law will be in creating a fair and honest mortgage marketplace until we have a fully functioning housing market. And unfortunately that won't happen until we effectively resolve the foreclosure crisis that continues to serve as an anchor on our housing market and on our overall economy.

The passage of Dodd-Frank

Beyond the creation of the Consumer Financial Protection Bureau (CFPB), I believe that the greatest impact Dodd-Frank will ultimately have is in its reform of the mortgage origination marketplace (once it's really functioning again). Of the problems I laid out earlier in my testimony, Dodd-Frank attempted to effectively address the key problems faced by consumers attempting to receive a fair and honest mortgage deal. Among the highlights:

1. Yield Spread Premiums Banned

The banning of yield spread premiums (YSPs) and other broker compensation based on the terms of a consumer's loan (except for the amount borrowed) may be the most important change to the mortgage origination landscape. No longer will mortgage brokers be allowed to benefit from steering consumers into loans with high rates or other terms lucrative for mortgage companies but harmful to consumers.

2. Forced Arbitration Clauses and Single-Premium Credit Insurance Banned;

While these anti-consumer provisions had been eliminated in much of the mortgage market, they still occasionally reared their ugly head in private label sponsored mortgages. Restoring a consumers right to hold mortgage banks accountable in court and finally putting an end to the abusive and costly practice of packing credit insurance on to a mortgage loan provide important protections for consumers.

3. *Limitation on Prepayment Penalties*

Another of one of the more abusive practices witnessed in the very recent mortgage market past, prohibiting prepayment penalties for subprime loans (as determined by a rate spread), adjustable-rate loans, and all loans that do not fit into "safe harbor" mortgages" should eliminate the problem of homeowners being trapped in expensive mortgage loans.

4. *The Ability-to-Repay Requirement*

Consumers were typically amazed (and appalled) when I explained that there was no federal law that prohibit mortgage originators from making loans that borrowers could not afford. Now that this has been remedied, I would hope that the mortgage industry would once again engage in fair and responsible underwriting of loans.

5. *The expansion of HOEPA*

Congress' original (and later the Federal Reserve Bureau's) definition of a high cost loan was simply too broad and allowed originators to make abusive loans that just skirted underneath the HOEPA defined limits. Through expanding the range of loans subject to HOEPA by lowering its triggers, by expanding the definition of points and fees and by creating a new trigger based solely on the timing or amount of prepayment penalties, and by adding important protections for consumers being sold a high-cost loan, the law provides consumers with much more robust protection from high cost loans.

6. *Appraisal Reform*

Phony appraisals were a source of great abuse and one of the reasons why so many homeowners today live with mortgages that exceed the value of their home. By imposing new restrictions on appraisals, including standards for appraisal independence and a prohibition on creditors extending mortgages if the creditor knows of a violation of these standards, the law took an important first step in protecting consumers from appraisal fraud.

7. *The creation of "Safe Harbor" Mortgages*

While the law, leaves the ultimate definition of "safe harbor" mortgages to the bank regulators it does lay out some extremely important guideposts. Among the standards that must be met for a mortgage to be "Qualified," the mortgage originator must document income and conduct an ability-to-pay analysis that considers taxes, insurance, and—for adjustable rate mortgages—the highest possible mortgage payment that could be required during the first five years of the loan. Additionally, to qualify for safe harbor status, loans generally cannot exceed thirty years and may not include negative amortization, a balloon payment, or points and fees exceeding 3%.

In an effort to hold investment banks accountable for the loans they help produce, the law also built in a 5% retention provision for these "securitizers" which can only be waived for loans that meet a substantive safe harbor at least as restrictive as the one described above (this is the Qualified Residential Mortgage standard that regulators are currently working on). Both the creation of an identifiably safe mortgage and a system where securitizers retain an interest in the mortgages they help create are extremely helpful to consumers looking to be treated fairly in the mortgage origination marketplace.

8. A Single, Integrated Disclosure

Dodd Frank requires the CFPB to create "a single, integrated disclosure" for mortgage transactions that combines the RESPA settlement statement and the mandatory TILA disclosures for mortgages. For more than a decade, federal regulators have struggled to createda fair and simple disclosure that gives consumers the essential information they need to both shop for a mortgage and then ultimately choose wisely for themselves. Each time HUD or the Federal Reserve attempted to develop a form that offered some promise for consumers, objections arose from various single-interest entities who feared that real, honest and consumer-friendly disclosures might hurt their bottom lines (i.e consumers would not choose their products or pay their inflated costs, if they actually understood what they were getting), and the effort failed.

This time, with a singularity of purpose, the CFPB has begun a fair and extremely open process to create a disclosure that actually meets the stated goals of RESPA and TILA, to help build a competitive mortgage market that allows informed consumers to actually shop for the best mortgage product. While the process has not yet been completed, we have been extremely impressed by both the empirical research conducted by the CFPB and the clarity and appropriateness of their initial disclosure prototypes. Of course, there is a long way to go in creating a final product, but it appears that the CFPB is well on its way to creating a binding TILA/RESPA integrated disclosure that will promote a fair, competitive and robust mortgage market.

Conclusion

Today, almost one year since the passage of the groundbreaking Dodd-Frank, our nation and hundreds of thousands of former and current homeowners, continue to struggle to right themselves. NACA strongly supports the mandates of Dodd-Frank whose greatest impact will be to reform the abuses in the mortgage origination marketplace. Homeownership remains a viable path to families building a positive economic future; many of the law's provisions, will safeguard minority, low and moderate income communities with the new consumer protection rules. NACA looks forward to the continued building of a strong watchdog agency in the Consumer Finance Protection Bureau.

NAIHP

Prepared Testimony of

Marc Savitt, CRMS
President

National Association of Independent Housing Professionals

On

"Mortgage Origination:
The Impact of Recent Changes on Homeowners and Businesses"

Before the

Committee on Financial Services,
Subcommittee on Insurance, Housing and Community Opportunity

United States House of Representatives

Wednesday, July 13, 2011

Good afternoon Chairwoman Biggert, Ranking Member Gutierrez, and Members of the Committee. I am Marc Savitt, President of the National Association of Independent Housing Professionals. Thank you for inviting NAIHP here today to testify on "Mortgage Origination: The Impact of Recent Changes on Homeowners and Businesses."

Chairwoman Biggert, we applaud you for providing this opportunity to testify about this important issue, which is critical to our housing recovery and the overall economic health of our country.

NAIHP represents independent, small business housing professionals in all 50 states and the District of Columbia. Our grassroots membership consists of mortgage brokers, loan originators, residential appraisers, real estate agents, settlement agents, small banks and consumers. Our members are Main Street USA, who assist consumers through the difficult maze of purchasing or refinancing residential real estate. We also provide jobs and contribute financially to our local economy.

For the past four years, two Administrations and Congress have sought the right solution to re-energize the housing industry. Despite the most affordable home prices and lowest interest rates in a generation, tax credits, and other incentives, our nation's housing market continues to underperform. Many speculate consumer confidence is the missing component to any housing recovery. While this is an important element, it is not a cure-all. Although unemployment also remains an obstacle, my testimony today pertains in part to the difficulties employed borrowers face in obtaining mortgage financing.

As a 30 year veteran of the mortgage financing industry, I can say without hesitation that the failure of the housing market to recover is the result of three main factors: Over-regulation, GSE guidelines and unnecessarily strict underwriting.

Overreaction to the housing crisis has resulted in over-regulation. Congress and the agencies have responded to the events of the last five plus years with harmful and often misguided regulations. Under the guise of consumer protection, these regulations were promulgated, despite overwhelming evidence of the dangers of unintended consequences. Many regulations call for restrictions on traditional mortgage products, such as conventional or government loans, which were never the problem.

Federal Reserve Board Rule on Mortgage Loan Originator Compensation

In one particularly onerous action by the Federal Reserve Board, the Central Bank finalized a rule on originator compensation, citing a certain practice by mortgage brokers to be unfair and deceptive. Regardless of the fact their study failed to substantiate their actions, the FRB still moved forward with the rule. The end result was massive job loss in the small business mortgage sector and elimination of consumer loan options.

As an active participant in meetings with the FRB during the comment period, it was evident the FRB was unwilling to listen to small business. Moreover, they ignored credible, independent studies from respected universities, which contradicted the findings of the FRB's limited study and outside survey.

The Federal Reserve Board based this anti-competitive rule on a "study" by MACRO International, which tested a total of 35 people in 4 cities. Furthermore, only 9 people of the 35 were tested on mortgage broker disclosures. In addition, the FRB also based this rule on a survey conducted by AARP. Just over one thousand people, aged 65 or older were called and asked questions about their mortgages. AARP admitted they never examined any loan documents from the survey. The entire compensation structure of the mortgage origination industry, which was based on competition, was changed to an anti-competitive, severely restricted industry, based on the opinions of 9 confused people.

The FRB chose to ignore two credible studies. The first was conducted by Georgetown University's Professor Gregory Elliehausen, titled "The Pricing of Subprime Mortgages by Mortgage Brokers and Lenders." This study included the <u>examination</u> of over one million subprime loans. The study concluded that consumers using a mortgage broker for home financing would save an average of 1.13% on their annual percent rate (APR). The study also dispelled the myth that mortgage brokers overcharged or took advantage of minorities. According to the findings of the study, minorities saved up to a full 2% on their APR. Ironically, Professor Elliehausen is now employed as an economist by the Federal Reserve Board.

The second study was performed by Harvard University, titled "Understanding the Boom and Bust in Nonprime Mortgage Lending." This study clearly examined the causes which lead to the housing crisis. The study found several contributing factors, including "relaxed underwriting" and "regulatory and market failures." It also specifically stated it was not caused by mortgage brokers and/or mortgage bankers.

Despite the research and findings of these extensive studies, the FRB chose to validate a study and survey that best matched the Central Banks desired outcome.

It should also be noted, according to the SBA's Office of Advocacy, the FRB failed to follow proper procedures in finalizing this rule, specifically the lack of a compliance guide that meets Advocacy standards. A compliance guide was eventually submitted, which consisted of a four page "cut and paste" out of the rule itself. By comparison, HUD submitted a 571 page compliance guide for RESPA Reform and currently has over 300 FAQ's. The FRB has no FAQ's.

The Office of Advocacy requested the FRB postpone implementation of the rule to allow small business to absorb the current "onslaught of regulations." The FRB ignored Advocacy's request.

The FRB also acknowledged the compensation rule would have a "significant economic impact on small entities." Despite having no idea how "significant" that impact would be, the rule was still implemented.

On March 7, 2011, NAIHP filed suit against the FRB in U.S. District Court in Washington, D.C. to stop the rule from being implemented on April 1, 2011. NAIHP's position was that the FRB lacked the authority to promulgate the rule, more specifically restrict compensation on traditional mortgages and that their testing was so flawed it was almost nonexistent. The court eventually deferred to the FRB on the authority issue because they claimed Congress's intent in Section 129(l) of TILA was unclear. Section 129 (l) refers to high cost mortgages only.

To be fair, the FRB held an on-line webinar on March 17, 2011, for the purpose of clarifying this confusing rule. However, all of the slides used by the FRB in the webinar contained a disclaimer which read, "The opinions expressed in this presentation are intended for informational purposes, and are not formal opinions, of nor binding on the Board of Governors of the Federal Reserve System."

This rule has left state regulators so confused, most refuse to enforce it. The FRB has also ignored repeated attempts by state regulators for clarification.

State Housing Finance Agencies, providers of low cost Mortgage Revenue Bonds (MRB) for first time homebuyers, are also adversely affected by this rule. The confusion over how to comply has lead to the termination of many wholesale relationships with mortgage brokers. Fewer originators of MRB's have caused the HFA's to lose substantial market share. Some HFA's are considering closing their doors. Consumers lose too with fewer originators in the market. Larger creditors often elect not to offer MRB's.

Most confusing of all was the FRB's acknowledgement in their answer to NAIHP's lawsuit that bank or creditor indirect compensation (YSP) was no different than broker yield spread premiums (YSP). The FRB stated both controlled the YSP and used it in the exact same manner. To reiterate, the FRB finalized this rule, because they believed broker YSP was an unfair and deceptive practice. NAIHP is puzzled by the FRB's logic, as they have made creditors exempt from this rule, despite their admission in a District Court filing, confessing that creditor (bank) and non-creditor (broker) yield spread premiums were identical. This admission is important for another reason, in that creditors most often deny receiving YSP or its equivalent, Service Release Premiums (SRP).

The FRB also claims this rule applies to creditors as well. In truth, the rule applies to creditor or bank originators, but not the creditors themselves. Banks are free to continue receiving both consumer and YSP compensation.

According to the FRB, this rule was enacted for consumer protection. However, in almost all cases the consumer still pays the same or a greater amount in settlement costs. Originator compensation has been reduced substantially with the reduction being retained by the creditor. This rule has no benefit to consumers.

Because the unintended consequences of this rule are so harmful to consumers and small business, NAIHP urges Congress to take the appropriate action to reverse it.

As the committee is aware, NAIHP submitted a proposed amendment to clarify the definition of a high cost mortgage and the intent of Congress under 129(l) of TILA, thereby clearing up any misunderstandings or ambiguity. This action would then limit the Originator Compensation Rule to only high cost mortgages, where it belongs.

RESPA Reform

In 2002, HUD began an initiative to "simplify and improve" the process for obtaining a home mortgage and reduce settlement costs for consumers. The centerpiece of that reform was a major revision of the Good Faith Estimate of Settlement Costs. During the comment period, HUD received over 45,000 comments, mostly in opposition to the changes. To be clear, industry agreed with HUD that changes were necessary to make the process easier for consumers to understand, thereby enabling them to make better and less expensive choices. However, the changes under the proposed rule actually made the process more complicated and confusing. After a two year debate, the proposed rule was withdrawn by HUD in March of 2004.

In 2005, HUD revisited the process of RESPA Reform by holding a series of seven roundtables throughout the country. The proposal was almost identical to the 2002 version. After numerous Congressional hearings and the required comment period, HUD finalized the rule, which was implemented on January 1, 2010.

The new GFE 2010, consisting of 3 pages, replaced a one page, totally itemized Good Faith Estimate. Instead of simplifying the process, HUD created a more confusing document, which amongst other things, fails to disclose a borrower's total housing payment, including taxes and insurance and the funds a borrower needs to bring to settlement. It also lacks a provision for a borrower's signature. To help remove the confusion, originators often use the old GFE, now called a "worksheet," as it clearly provides a complete picture of the costs involved with the borrower's transaction. While we applaud HUD for recognizing the need for true simplification, the GFE 2010 fell short of achieving that goal.

The CFPB apparently understands the problem and is in the process of developing a new combined Good Faith Estimate and Truth in Lending disclosure.

RESPA Reform also included a revision to the section concerning Controlled Business Arrangements (CBA's), sometimes called Affiliated Business Arrangements (AfBA's). The revision further clarified the prohibition on tying arrangements. HUD recognized the growing problems with these arrangements, specifically where buyers were required to use the services of the builder's affiliated companies in order to receive discounts and incentives. These requirements prevent consumers from shopping for a home loan best suited for them. Builders and lenders in a joint venture relationship routinely offer discounts and incentives to home buyers, provided the consumer uses the services of the builder's chosen settlement service provider. In other words, if the buyer uses an outside mortgage lender and/or settlement agent, they forfeit the discounts and incentives.

These so-called "one stop shops," have not only proven to be harmful to consumers by way of higher settlement costs, but have shown to be a major cause of foreclosures.

Buyers were regularly promised closing cost assistance, upgraded kitchens, swimming pools and other incentives. Although buyers received closing cost estimates from the builder's affiliate with low interest rates, those rates usually disappeared when the consumer was able to lock in their interest rate. In many cases, rate variations of more than one full percent were experienced. If the consumers elected to forfeit the incentives and use a less expensive, outside service provider, builders required immediate payment of all "free" upgrades, or warned contracts would be terminated for breach and deposits lost. Consumers were locked into a bad deal with no way out.

These arrangements are harmful to both consumers and small business. Local small business professionals are frozen out of the new home industry, in favor of the large national banks.

Prior to implementation of this specific section of RESPA Reform, numerous home builders successfully sued HUD, winning a stay. HUD later withdrew the provision and promised to revisit it in the near future.

The GSE Guidelines

For many years, the GSE's set the underwriting standards for the majority of the mortgage financing industry. Their standards were conservative, with the goal of protecting both industry and borrowers. However, early in the last decade they began taking unnecessary risks in order to regain lost market share. Some of those risks included the lowering of prudent underwriting standards and implementation of non-prime lending programs.

Although relaxing their guidelines opened the door to home ownership for more borrowers, many of those borrowers proved to be unqualified. We're all experiencing the end result of those failures by the GSE's.

Today, the GSE's are overcompensating for their mistakes of the past. Underwriting standards and conditions have reached the level of absurd. Moreover, the GSE's are penalizing new borrowers with predatory fees to recoup losses related to their previous practices. Borrowers are assessed fees for adverse market, credit scores below 740, loan to values, ratios and much more. In some cases, GSE fees add up to between 5-6% of the loan amount. If a mortgage broker or banker charged these kinds of fees, they would face regulatory action.

Industry concurs, if the GSE guidelines were revised to reflect a more common sense approach, while still being prudent, more qualified borrowers would be eligible for home financing. Reduction, if not removal of the predatory fees charges by the GSE's, would also make financing more affordable.

The GSE's and the Home Valuation Code of Conduct

The Home Valuation Code of Conduct (HVCC) was an agreement between the N.Y. Attorney General, Fannie Mae, Freddie Mac and their regulator FHFA.

HVCC was born from an investigation of a federally chartered bank and an unregulated appraisal management company. The investigation revealed conflicts of interest and the influencing of appraisers to fraudulently inflate the value of real estate.

The following paragraph is an exact quote from former N.Y. Attorney General Andrew Cuomo's own website.

"In 2007 Cuomo also announced an investigation into widespread appraisal fraud within the mortgage industry, examining practices used by some of the country's largest banks of pressuring appraisers to artificially inflate the value of homes. As a result of these investigations, Fannie Mae and Freddie Mac, the largest purchasers of home loans, agreed to abide by new appraisal guidelines defined by the Attorney General and to fund an Independent Valuation Protection Institute to implement and monitor those guidelines."

In March of 2008, the original (proposed) HVCC agreement prohibited banks and lenders from having more than a 20% interest in appraisal management companies (AMC). Moreover, mortgage brokers were prohibited from ordering or having any contact with the appraisal process. When the final version of HVCC was released in December of 2008, the banks 20% ownership cap was removed, allowing banks and lenders to own an unlimited percentage of interest in AMC's.

After numerous meetings with Mr. Cuomo's staff, NAIHP was informed the revisions were made at the insistence of the FHFA, regulator for the GSE's. NAIHP questions why Mr. Cuomo would allow the banks and lenders back into the exact situation that first caused him to initiate his investigation. The very banks and AMC's from his investigation were now in control of the residential valuation system in this country. Despite the fact mortgage brokers were NOT the subject of his investigation, the December 2008 final agreement required their removal from the appraisal process.

Since HVCC went into effect on May 1, 2009, consumers have incurred substantial additional expenses when purchasing or refinancing residential properties. It is conservatively estimated those costs exceed 2.8 Billion dollars a year. Most importantly, HVCC has done nothing to reduce fraud and/or conflicts of interest. In fact, statistics have shown valuation fraud increased

46% in the 3rd quarter of 2009, as compared to the same time in 2008. In the spring of 2010 and 2011, the Mortgage Asset Research Institute (MARI), reported valuation fraud had increased over 50%, year over year. This substantial increase occurred despite HVCC.

The agreement between the N.Y. Attorney General and the GSE's has sunset. However, the exact same provisions within HVCC are now embedded in the GSE guidelines and the Dodd-Frank Wall Street Reform and Consumer Protection Act. Now known as "Appraiser Independence", it can be found under Section 1472.

In addition to valuation fraud increasing at alarming rates, appraiser independence (AP) has also caused thousands of appraisers to go out of business. Local small business appraisers have lost their independence to unregulated AMC's. Appraisers can no longer set their fees. Fees are dictated by the AMC's and often end up being between 40%-60% less than what is customary and reasonable for a specific geographic area. Sometimes, appraisal assignments are put up for bid. It is important to understand consumer costs have not been reduced along with appraiser compensation. In fact, the cost of an appraisal has increased on average $150.00. The increase, along with the "haircut" taken by appraisers, has gone into the pockets of AMC's and their partners, the big banks.

The long term outlook for the appraisal industry is even worse. Because appraiser compensation has been drastically reduced, they can no longer afford to hire an apprentice. An apprentice needs a minimum of 2000 hours working under a licensed appraiser before they can be licensed. The average age of an appraiser is 56, which means within 8-10 years the appraisal industry will be a fraction of what it is today.

Under the current system of hiring the least expensive appraiser, including those unfamiliar with the subject property's geographic area, quality and accurate workmanship are often sacrificed.

Dodd-Frank

The Consumer Financial Protection Bureau (CFPB) is currently in the testing stage of a new, combined Good Faith Estate of Settlement Costs and Truth in Lending Statement. The CFPB should be applauded for not only taking on this much needed disclosure reform, but also for the process. The housing industry and consumers have been involved since the earliest stages of development and have been asked for their input every step of the way. Unlike other agencies, CFPB actually used this input to make changes and corrections to early drafts. This kind of cooperation reduces the chances of unintended consequence, after implementation.

The name, The Dodd-Frank Wall Street Reform and Consumer Protection Act (DFA), is misleading at best. While promoted as a vehicle to prevent systemic risk and prevent further bailouts of those who are "too big to fail," it appears to have left Wall Street and big bank practices virtually intact, all at the expense of small business and consumers. As with many laws designed to protect consumers, they end up having the opposite effect. In the case of the DFA, a rush to judgment and an intense lobbying campaign by big banks has all but eliminated competition. Consumers now have less choice and/or options.

Late in the evening, during the Senate debate of the DFA, Senators Jeff Merkley and Amy Klobuchar introduced an amendment pertaining to loan originator compensation and a borrower's ability to repay a loan. While NAIHP completely agrees that borrowers must be able to afford their home loan financing, we take exception with the originator compensation issue, in particular the way this amendment was introduced. After its introduction that evening, it was quickly voted on the next morning. Small business mortgage brokers were not given the opportunity to discuss the amendment prior to introduction or voting. Had brokers and originators been given the opportunity, we would have identified several areas of concern pertaining to both consumer and small business harm.

For example, brokers are prohibited from receiving compensation from both the wholesale lender and the consumer. Arguments have been made by consumer groups, legislators and others that this practice increases consumer costs and is a kickback to brokers. Brokers have been fighting this illusionary issue on yield spread premiums for years. What opponents of YSP fail to admit is this form of compensation is legal, legitimate and necessary to help qualified borrowers. Moreover, as recently acknowledged by the Federal Reserve Board, creditors (banks), receive the exact same type of compensation. The only difference is brokers disclose all their compensation to consumers. Banks have no such requirement.

DFA and Restoring Appraiser Independence

Appraiser independence requirements were established under the DFA to ensure that residential real estate appraisals are based on an appraiser's independent professional judgment, free of any influence, pressure or coercion from parties who have an interest in the transaction. The requirements under the interim rule established by the Federal Reserve Board also seek to ensure that appraisers are paid "Customary and Reasonable fees."

Unfortunately, like its predecessor HVCC, appraiser independence has already proven to be a failure. Appraisers are still being pressured and blacklisted with no mechanism in place to report offenses. Moreover, Appraisal Management Companies (AMC's), have found a "workaround" enabling them to set factious "Customary and Reasonable fees," that are anything but customary and reasonable. In fact, appraisers are now being paid less than under HVCC.

Although, specific language is not clear in the interim rule, the FRB has verbally confirmed mortgage brokers are NOT prohibited from ordering residential real estate appraisals. NAIHP believes Congress should confirm this with the FRB.

During the DFA conference committee, a bipartisan amendment was offered by Rep. Gary Miller of CA and Rep. Travis Childers of MS. This amendment would have restored the appraisal ordering process to mortgage brokers and loan originators. The amendment was accepted by the House, but specifically singled out and rejected by Senator Dodd.

Restoring the right of mortgage brokers and loan originators to order appraisals and converse with appraisers is paramount to restoring true appraiser independence in our valuation system. Like the larger housing crisis itself, mortgage brokers were painted as the villains of appraiser pressure and coercion. However, under the equivalent guidelines of HVCC, brokers were proven NOT to be the "bad actors." Though some brokers were involved, as an industry, they were scapegoats. Since May 1, 2009, brokers have been prohibited from any involvement with appraisers, including ordering appraisals. During this same time frame, appraisal fraud increased over 50%. This clearly vindicates brokers, because they were out of the process.

Brokers were excluded from the process because it was said that they benefited financially from the transactions. While this is true, almost every case prosecuted for influence, pressure and/or fraud has been against banks and those who have joint venture relationships with AMC's.

Another reason to allow mortgage brokers and their loan originators back into the appraisal system is they are now licensed under the SAFE Act. In addition to this rigid approval process, every document handled by a licensed broker or originator has their NLMS number displayed. If a licensed individual were to engage in a pattern of practice of committing any offense, regulators would easily be able to identify the originator and take appropriate action.

Qualified Residential Mortgages (QRM)

Once again, regulators fail to see the unintended consequences of their actions. Instead of conducting an independent GAO study to determine need, regulators appear to be engaged in overkill regulation.

Requiring a 20% down payment will preclude most first time, low and moderate income buyers from ever having a home of their own. Saving for this large of a down payment is difficult at best for most buyers and impossible for others. Moreover, the down payment was never the problem with qualified buyers. In fact, the two best performing loan programs are the Veterans Administration (VA) and the USDA Rural Housing Program. Both offer 100% financing to qualified borrowers.

Loose underwriting standards, including no documentation loans for average wage and hour employees, were a major contributing factor to the housing crisis.

NAIHP is concerned that if the 20% down payment requirement is finalized, the ripple effect from a further weakened housing industry will cause home prices to plummet, while unemployment and foreclosures rise sharply.

Mortgage Brokers and Loan Originators

From the very moment mainstream media first used the words "mortgage meltdown," mortgage brokers were labeled as the group that inflicted the predatory practices that gave rise to record foreclosures. As a result, mortgage brokers have been subjected to intense scrutiny and, consequently, anti-competitive rules and regulations.

Brokers have been blamed for putting consumers into predatory loan programs. In reality, mortgage brokers never developed one single loan product or program. However, many lenders and banks did, aided by Fannie Mae, Freddie Mac and Wall Street. These same institutions set the guidelines for such programs, without any broker input. Most importantly, mortgage brokers did not underwrite or approve any of these loans. The responsibility for approving loans was that of the banks and lenders. Therefore, if brokers didn't develop the programs, set the guidelines or approve loans, how could this be their fault?

Ironically, many of the rules and regulations promulgated against mortgage brokers, under the guise of consumer protection, have resulted in further consumer harm and job loss in the small business housing sector. Reduced competition has increased costs for consumers, along with a substantial rise in fraud.

Numerous independent studies have provided empirical evidence, establishing the true facts of what caused the mortgage meltdown and housing crisis. Agency rules and regulations were written based on flawed, or no testing and anecdotal evidence, often provided by consumer groups and banks with ulterior motives.

As a result of the SAFE Act, mortgage brokers and their loan originators are now some of the most highly regulated and educated mortgage professionals in the industry. NAIHP believes any mortgage professional engaged in the practice of originating residential mortgages should be required to meet the same licensing standards.

NAIHP looks forward to continuing to work with this committee, and other House members, to improve our housing industry.

Thank you for the opportunity to appear before the committee and discuss these important issues.

United States Government Accountability Office

GAO

Testimony

Before the Subcommittee on Insurance, Housing and Community Opportunity, Committee on Financial Services, House of Representatives

For Release on Delivery
Expected at 2:00 p.m. EDT
Wednesday, July 13, 2011

RESIDENTIAL APPRAISALS

Opportunities to Enhance Oversight of an Evolving Industry

Statement of William B. Shear, Director
Financial Markets and Community Investment

U.S. Government Accountability Office
GAO 90 YEARS 1921-2011
ACCOUNTABILITY ★ INTEGRITY ★ RELIABILITY

GAO-11-783T

Chairman Biggert, Ranking Member Gutierrez, and Members of the Subcommittee:

I am pleased to be here today to discuss our work on residential real estate valuations. Real estate valuations, which encompass appraisals and other value estimation methods, play a critical role in mortgage underwriting by providing evidence that the market value of a property is sufficient to help mitigate losses if the borrower is unable to repay the loan. However, recent turmoil in the mortgage market has raised questions about mortgage underwriting practices, including the quality and credibility of some valuations. An investigation into industry appraisal practices by the New York State Attorney General led to an agreement in 2008 between the Attorney General; Fannie Mae and Freddie Mac (the enterprises); and the Federal Housing Finance Agency (FHFA), which regulates the enterprises. This agreement included the Home Valuation Code of Conduct (HVCC), which set forth certain appraiser independence requirements for loans sold to the enterprises and took effect in 2009. The Dodd-Frank Wall Street Reform and Consumer Protection Act (Pub. L. No. 111-203) (the Dodd-Frank Act) directed us to study the effectiveness and impact of various valuation methods and the options available for selecting appraisers, as well as the impact of HVCC.[1]

My statement summarizes the report we are releasing today, which responds to the mandate in the Dodd-Frank Act.[2] Our work focused on valuations of single-family residential properties for first-lien purchase and refinance mortgages. The report discusses (1) the use of different valuation methods and their advantages and disadvantages, (2) policies and other factors that affect consumer appraisal costs and requirements for lenders to disclose appraisal costs and valuation reports to consumers, and (3) conflict-of-interest and appraiser selection policies and views on the impact of these policies on industry stakeholders and appraisal quality. We consider the impact of HVCC throughout the report. To do this work, we analyzed proprietary data we obtained from the enterprises, lenders, and a mortgage technology company on the use of different valuation methods and appraisal approaches.[3] We reviewed

[1]Dodd-Frank Act § 1476.

[2]GAO, *Residential Appraisals: Opportunities to Enhance Oversight of an Evolving Industry*, GAO-11-653 (Washington, D.C.: July 13, 2011).

[3]See GAO-11-653 for more information about the data we obtained for this study.

academic and industry literature and examined federal regulations and policies, as well as internal policies and procedures of lenders. Finally, we interviewed a broad range of appraisal and mortgage industry participants and observers and discussed these issues with officials from the enterprises, FHFA, the federal banking regulatory agencies, and other federal agencies. The work that this statement is based on was performed from July 2010 to July 2011 in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

The Widespread Use of Appraisals for Mortgage Originations Reflects Their Advantages Relative to Other Valuation Methods

Available data and interviews with lenders and other mortgage industry participants indicate that appraisals are the most frequently used valuation method for home purchase and refinance mortgage originations. Appraisals provide an opinion of market value at a point in time and reflect prevailing economic and housing market conditions.[4] Data provided to us by the five largest lenders (measured by dollar volume of mortgage originations in 2010) show that, for the first-lien residential mortgages for which data were available, these lenders obtained appraisals for about 90 percent of the mortgages they made in 2009 and 2010, including 98 percent of home purchase mortgages. The data we obtained from lenders include mortgages sold to the enterprises and mortgages insured by the Federal Housing Administration (FHA), which together accounted for the bulk of the mortgages originated in 2009 and 2010. The enterprises and FHA require appraisals to be performed for a large majority of the mortgages they purchase or insure. For mortgages for which an appraisal was not done, the lenders we spoke with reported that they generally relied on validation of the sales price (or loan amount in the case of a refinance) against a value generated by an automated valuation model (AVM), in accordance with enterprise policies

[4]The enterprises and federal banking regulators define market value as the most probable price that a property should bring in a competitive and open market under all conditions requisite to a fair sale, the buyer and seller each acting prudently and knowledgeably, and assuming the price is not affected by undue stimulus.

that permit this practice for some mortgages with characteristics associated with a lower default risk.[5]

The enterprises, FHA, and lenders require and obtain appraisals for most mortgages because appraising is considered by mortgage industry participants to be the most credible and reliable valuation method for a number of reasons. Most notably, appraisals and appraisers are subject to specific requirements and standards. In particular, the Uniform Standards of Professional Appraisal Practice (USPAP) outlines the steps appraisers must take in developing appraisals and the information appraisal reports must contain.[6] USPAP also requires that appraisers follow standards for ethical conduct and have the competence needed for a particular assignment. Furthermore, state licensing and certification requirements for appraisers include minimum education and experience criteria, and standardized report forms provide a way to report relevant appraisal information in a consistent format.

In contrast, other valuation methods, such as broker price opinions (BPO) and AVMs, are not permitted for most purchase and refinance mortgage originations.[7] The enterprises do not permit lenders to use BPOs for mortgage originations and only permit lenders to use AVMs for a modest percentage of mortgages they purchase. Additionally, the federal banking regulators' guidelines state that BPOs and AVMs cannot be used as the primary basis for determining property values for mortgages originated by regulated institutions. However, the enterprises and lenders use BPOs and AVMs in a number of circumstances other than purchase and refinance mortgage originations because these methods can provide quicker, less expensive means of valuing properties in active markets.

When performing appraisals, appraisers can use one or more of three approaches to value—sales comparison, cost, and income. The sales comparison approach compares and contrasts the property under

[5]An AVM is a computerized model that estimates property values using public record data, such as tax records and information kept by county recorders, multiple listing services, and other real estate records.

[6]The Appraisal Standards Board of the Appraisal Foundation develops, interprets, and amends USPAP. The Appraisal Foundation is a not-for-profit organization established by the appraisal profession in 1987.

[7]A BPO is an estimate of the probable selling price of a particular property prepared by a real estate broker, agent, or sales person rather than by an appraiser.

appraisal with recent offerings and sales of similar properties. The cost approach is based on an estimate of the value of the land plus what it would cost to replace or reproduce the improvements minus depreciation. The income approach is an estimate of what a prudent investor would pay based upon the net income the property produces. USPAP requires appraisers to consider which approaches to value are applicable and necessary to perform a credible appraisal and provide an opinion of the market value of a particular property. Appraisers must then reconcile values produced by the different approaches they use to reach a value conclusion.

The enterprises and FHA require that, at a minimum, appraisers use the sales comparison approach for all appraisals because it is considered most applicable for estimating market value in typical mortgage transactions. Consistent with these policies, our review of valuation data that we obtained from a mortgage technology company—representing about 20 percent of mortgage originations in 2010—indicates that appraisers used the sales comparison approach for nearly all (more than 99 percent) of the mortgages covered by these data. The cost approach, which was generally used in conjunction with the sales comparison approach, was used somewhat less often—in approximately two-thirds of the transactions in 2009 and 2010, according to these data. The income approach was rarely used. Some mortgage industry stakeholders have argued that wider use of the cost approach in particular could help mitigate what they view as a limitation of the sales comparison approach. They told us that reliance on the sales comparison approach alone can lead to market values rising to unsustainable levels and that using the cost approach as a check on the sales comparison approach could help lenders and appraisers identify when this is happening. For example, these stakeholders pointed to a growing gap between average market values and average replacement costs of properties as the housing bubble developed in the early to mid-2000s. However, other mortgage industry participants noted that a rigorous application of the cost approach may not generate values much different from those generated using the sales comparison approach. They indicated, for example, that components of the cost approach—such as land value or profit margins of real estate developers—can grow rapidly in housing markets where sales prices are increasing. The data we obtained did not allow us to analyze the differences between the values appraisers generated using the different approaches.

Recent Policy Changes May Affect Consumer Costs for Appraisals, while Other Policy Changes Have Enhanced Disclosures to Consumers

Factors such as the location and complexity of the property affect consumer costs for appraisals. For example, a property may have unique characteristics that are more difficult to value, such as being much larger than nearby properties or being an oceanfront property, which may require the appraiser to take more time to gather and analyze data to produce a credible appraisal. Mortgage industry participants we spoke with told us that the amount a consumer pays for an appraisal is generally not affected by whether the lender engages an appraiser directly or uses an appraisal management company (AMC)—which manages the appraisal process on lenders' behalf—to select an appraiser.[8] They said that AMCs typically charge lenders about the same amount that independent fee appraisers would charge lenders directly, and lenders generally pass on these charges to consumers. In general, lenders, AMC officials, appraisers, and other industry participants noted that consumer costs for appraisals have remained relatively stable in the past several years. However, appraisers have reported receiving lower fees when working with AMCs compared with working directly with lenders because AMCs keep a portion of the total fee.

A provision in the Dodd-Frank Act that requires lenders to pay appraisers a customary and reasonable fee could affect consumer costs and appraisal quality, depending on interpretation and implementation of federal rules.[9] The effect of this change on consumer costs may depend on the approach lenders and AMCs take in order to demonstrate compliance. For example, some lenders and industry groups are having fee studies done to determine what constitutes customary and reasonable fees. According to the Dodd-Frank Act, these studies cannot include the fees AMCs pay to appraisers. As a result, some industry participants, including some AMC officials, expect these studies to demonstrate that appraiser fees should be higher than what AMCs are currently paying. If that is the case, these lenders would require AMCs to increase the fees they pay to appraisers to a rate consistent with the findings of those studies, which in turn could increase appraisal costs for consumers. However, some lenders are evaluating the possibility of no longer using AMCs and engaging appraisers directly, which would eliminate the AMC administration fee from the appraisal fee that consumers pay.

[8]AMCs perform a number of specific functions for lenders, including recruiting, selecting, and contracting with appraisers.

[9]Dodd-Frank Act § 1472(a) (codified at 15 U.S.C. § 1639e(i)).

Other recent policy changes that took effect in 2010 aim to provide lenders with a greater incentive to estimate costs accurately when providing consumers with an estimated price for third-party settlement services, including appraisals. If actual costs exceed estimated costs by more than 10 percent, the lender is responsible for making up the difference. The Dodd-Frank Act permits, but does not require, lenders to separately disclose to consumers the fee paid to the appraiser by an AMC and the administration fee charged by the AMC.[10] Another policy change enhances disclosures by requiring lenders to provide consumers with a copy of the valuation report prior to closing.

Conflict-of-Interest Policies Have Changed Appraiser Selection Processes, with Implications for Appraisal Oversight

Recently issued policies reinforce long-standing requirements and guidance designed to address conflicts of interest that may arise when direct or indirect personal interests bias appraisers from exercising their independent professional judgment. In order to prevent appraisers from being pressured, the federal banking regulators, the enterprises, FHA, and other agencies have regulations and policies governing the selection of, communications with, and coercion of appraisers. Examples of recently issued policies that address appraiser independence include HVCC, which took effect in May 2009; the enterprises' new appraiser independence requirements that replaced HVCC in October 2010; and revised *Interagency Appraisal and Evaluation Guidelines* from the federal banking regulators, which were issued in December 2010. Provisions of these and other policies address (1) prohibitions against loan production staff involvement in appraiser selection and supervision; (2) prohibitions against third parties with an interest in the mortgage transaction, such as real estate agents or mortgage brokers, selecting appraisers; (3) limits on communications with appraisers; and (4) prohibitions against coercive behaviors.

According to mortgage industry participants, HVCC and other factors have contributed to changes in appraiser selection processes—in particular, lenders' more frequent use of AMCs to select appraisers.[11] Some appraisal industry participants said that HVCC, which required

[10]Dodd-Frank Act § 1475 (codified at 12 U.S.C. § 2603).

[11]Although industry-wide data on lenders' use of AMCs over time are unavailable, appraisal industry participants told us that between 60 and 80 percent of appraisals are currently ordered through AMCs. They provided varying estimates of AMC use prior to HVCC, ranging from 15 percent to 50 percent of mortgage originations.

additional layers of separation between loan production staff and appraisers for mortgages sold to the enterprises, led some lenders to outsource appraisal functions to AMCs because they thought using AMCs would allow them to easily demonstrate compliance with these requirements. In addition, lenders and other mortgage industry participants told us that market conditions, including an increase in the number of mortgages originated during the mid-2000s, and lenders' geographic expansion over the years, put pressure on lenders' capacity to manage appraisers and led to their reliance on AMCs.

Greater use of AMCs has raised questions about oversight of these firms and their impact on appraisal quality. Direct federal oversight of AMCs is limited. Federal banking regulators' guidelines for lenders' own appraisal functions list standards for appraiser selection, appraisal review, and reviewer qualifications. The guidelines also require lenders to establish processes to help ensure these standards are met when lenders outsource appraisal functions to third parties, such as AMCs. Officials from the federal banking regulators told us they review lenders' policies and controls for overseeing AMCs, including the due diligence they perform when selecting AMCs. However, they told us they generally do not review an AMC's operations directly unless they have serious concerns about the AMC and the lender is unable to address those concerns. In addition, a number of states began regulating AMCs in 2009, but the regulatory requirements vary and provide somewhat differing levels of oversight, according to officials from several state appraiser regulatory boards.

Some appraiser groups and other appraisal industry participants have expressed concern that existing oversight may not provide adequate assurance that AMCs are complying with industry standards. These participants suggested that the practices of some AMCs for selecting appraisers, reviewing appraisal reports, and establishing qualifications for appraisal reviewers—key areas addressed in federal guidelines for lenders' appraisal functions—may have led to a decline in appraisal quality. For example, appraiser groups said that some AMCs select appraisers based on who will accept the lowest fee and complete the appraisal report the fastest rather than on who is the most qualified, has the appropriate experience, and is familiar with the relevant neighborhood. AMC officials we spoke with said that they have processes that address these areas of concern—for example, using an automated system that identifies the most qualified appraiser based on the requirements for the assignment, the appraiser's proximity to the subject property, and performance metrics such as the timeliness and quality of the appraiser's work.

While the impact of the increased use of AMCs on appraisal quality is unclear, Congress recognized the importance of additional AMC oversight in enacting the Dodd-Frank Act by placing the supervision of AMCs with state appraiser regulatory boards. The Dodd-Frank Act requires the federal banking regulators, FHFA, and the Bureau of Consumer Financial Protection to establish minimum standards for states to apply in registering AMCs, including requirements that appraisals coordinated by an AMC comply with USPAP and be conducted independently and free from inappropriate influence and coercion.[12] This rulemaking provides a potential avenue for reinforcing existing federal requirements for key functions that may impact appraisal quality, such as selecting appraisers, reviewing appraisals, and establishing qualifications for appraisal reviewers. Such reinforcement could help to provide greater assurance to lenders, the enterprises, and federal agencies of the quality of the appraisals provided by AMCs.

To help ensure more consistent and effective oversight of the appraisal industry, the report we are issuing today recommends that the heads of the federal banking regulators (FDIC, the Federal Reserve, NCUA, and OCC), FHFA, and the Bureau of Consumer Financial Protection—as part of their joint rulemaking required under the Dodd-Frank Act—consider including criteria for the selection of appraisers for appraisal orders, review of completed appraisals, and qualifications for appraisal reviewers when developing minimum standards for state registration of AMCs. In written comments on a draft of our report, the federal banking regulators and FHFA agreed with or indicated they will consider this recommendation. The Bureau of Consumer Financial Protection did not receive the draft report in time to provide comments.

Chairman Biggert, Ranking Member Gutierrez, and Members of the Subcommittee, this concludes my prepared statement. I am happy to respond to any questions you may have at this time.

[12]Dodd-Frank Act § 1473(f)(2) (codified at 12 U.S.C. § 3353(a)).

GAO Contact and Staff Acknowledgments

For further information on this testimony, please contact me at (202) 512-8678 or shearw@gao.gov. Contact points for our Offices of Congressional Relations and Public Affairs may be found on the last page of this statement. Key contributors to this testimony include Steve Westley, Assistant Director; Don Brown; Marquita Campbell; Anar Ladhani; John McGrail; Erika Navarro; Jennifer Schwartz; and Andrew Stavisky.

GAO's Mission

The Government Accountability Office, the audit, evaluation, and investigative arm of Congress, exists to support Congress in meeting its constitutional responsibilities and to help improve the performance and accountability of the federal government for the American people. GAO examines the use of public funds; evaluates federal programs and policies; and provides analyses, recommendations, and other assistance to help Congress make informed oversight, policy, and funding decisions. GAO's commitment to good government is reflected in its core values of accountability, integrity, and reliability.

Obtaining Copies of GAO Reports and Testimony

The fastest and easiest way to obtain copies of GAO documents at no cost is through GAO's Web site (www.gao.gov). Each weekday afternoon, GAO posts on its Web site newly released reports, testimony, and correspondence. To have GAO e-mail you a list of newly posted products, go to www.gao.gov and select "E-mail Updates."

Order by Phone

The price of each GAO publication reflects GAO's actual cost of production and distribution and depends on the number of pages in the publication and whether the publication is printed in color or black and white. Pricing and ordering information is posted on GAO's Web site, http://www.gao.gov/ordering.htm.

Place orders by calling (202) 512-6000, toll free (866) 801-7077, or TDD (202) 512-2537.

Orders may be paid for using American Express, Discover Card, MasterCard, Visa, check, or money order. Call for additional information.

To Report Fraud, Waste, and Abuse in Federal Programs

Contact:

Web site: www.gao.gov/fraudnet/fraudnet.htm
E-mail: fraudnet@gao.gov
Automated answering system: (800) 424-5454 or (202) 512-7470

Congressional Relations

Ralph Dawn, Managing Director, dawnr@gao.gov, (202) 512-4400
U.S. Government Accountability Office, 441 G Street NW, Room 7125
Washington, DC 20548

Public Affairs

Chuck Young, Managing Director, youngc1@gao.gov, (202) 512-4800
U.S. Government Accountability Office, 441 G Street NW, Room 7149
Washington, DC 20548

Please Print on Recycled Paper

Testimony of Sara W. Stephens, MAI, CRE

Mortgage Origination: The Impact of Recent Changes on Homeowners and Businesses

House Committee on Financial Services
Subcommittee on Insurance, Housing and Community Opportunity

Washington Office
Appraisal Institute
122 C Street, NW, Suite 360
Washington, DC 20001
202-298-6449

Headquarters
Appraisal Institute
555 W. Van Buren Street, Suite 1000
Chicago, IL 60607
312-335-4100

July 13, 2011

Madam Chair, members of the Subcommittee, thank you for the opportunity to share our thoughts regarding the appraisal process and residential mortgage origination on behalf of the nearly 25,000 members of the Appraisal Institute, the largest professional association of real estate appraisers in the United States. Despite severe economic and industry challenges, real estate appraisers, everyday, are helping financial institutions, consumers, government agencies and investors understand risks in the real estate market. Collateral risk assessment is one of the cornerstones of mortgage lending, and today's complex markets are presenting unique challenges that professional appraisers can help to clarify.

Despite this work, we believe the work of appraisers is vastly underutilized by mortgage lenders today, and facing severe strain as a result of a conflicted and burdensome regulatory environment. Real estate appraisers are professional analysts of real property markets. They are trained to research and investigate the behaviors of buyers and sellers in the market. An appraisal is a *professional service*. It is not like a flood certification, which can be generated by a click of a button. Credible appraisals require research, analysis, inspection and rigorous training. They require competence, independence, and ethics.

However, many mortgage lenders, and sadly, some government agency officials, fail to recognize this distinction, helping to promote commoditization of appraisals, as if they were all the same or created equally. Rather than analysts, appraisers are at risk of becoming glorified data aggregators and form fillers, thanks partly, to government policies. Rather than conducting rigorous valuations of collateral, many lenders are quickly reinforcing practices that promote "collateral validation," focusing more on the form than on the content or analysis. We believe that such views helped to create the mortgage crisis of recent years, and that a continuation of these practices will place us at great risk in the future.

Last year, Congress passed the most significant legislative update of the appraisal regulatory structure in two decades. In our view, this was only a beginning. Moving forward, Congress must maintain an active role in oversight of appraisal regulators and build on these reforms to address ongoing weaknesses. We can ill afford to allow another twenty years to pass without a thorough audit of appraisal regulations. Consumers, lenders, and taxpayers deserve much better than they have been given to date.

Our testimony is divided into two sections. Part I outlines concerns regarding the substance of appraisal policies; Part II outlines concerns regarding "process" and appraisal regulatory oversight.

Part 1: Promoting Development of Credible Appraisals and Protecting and Informing Consumers

A. **The Consumer Financial Protection Bureau (CFPB) must correct the Interim Final Rule on appraisal independence and implement the intent of the Dodd-Frank Act**

On April 1, one of the first rules resulting from the Dodd-Frank Act took effect. Known as the Interim Final Rule on Truth in Lending, and specifically on appraisal independence, the rule carries over many provisions from the Home Valuation Code of Conduct (HVCC) to apply to all consumer mortgage transactions. It also mandated the requirement of payment of customary and reasonable fees to appraisers. Until enactment of the HVCC, this rule was unneeded. The system operated freely with each appraiser setting fees based on their education, experience and assignment conditions. The HVCC, unfortunately, created an environment more consistent with an oligopoly; a handful of middleman management companies which presently control approximately 70% of appraisal orders.

Unfortunately, the Federal Reserve Board issued a rule that fails to implement the plain language and public policy intent of defining reasonable and customary fees as those not involving appraisal management companies – a retail fee, if you will. In our view, the reason Congress included this provision in the Dodd-Frank Act is to help ensure that appraisers receive adequate compensation for the education, experience, and time necessary to prepare credible appraisal reports. While the price of any service will always be a factor, quality and competency and transparency to the consumer should come first. Business models that helped fuel the fundamentally unsound run-up of the past decade placed far too much emphasis on pricing and bundling of services and focused scant attention on appraisal quality. Congress got it right; unfortunately, the Federal Reserve got it wrong.

As implemented, the Interim Final Rule contains "two presumptions of compliance" that have no statutory basis. In sum, the first presumption simply reaffirms the status quo business model that crams down fees on appraisers; the second presumption is relatively consistent with the Dodd-Frank Act, but is made secondary by failing to include a safe harbor.

The origins of the two presumption system are unclear, but the result is simple. The two presumption system enables the oligopolistic-like system to maintain its status quo to the detriment of the safety and soundness of the banking system. Nowhere in the Dodd-Frank Act did Congress imply any presumptions of compliance, and Dodd-Frank certainly did not imply that customary and reasonable fees should involve assignments involving known appraisal management companies. Rather, Dodd-Frank very clearly defines such fees as those absent the involvement of known appraisal management companies.

Specifically, Dodd-Frank states:

> *Lenders and their agents shall compensate fee appraisers at a rate that is customary and reasonable for appraisal services performed in the market area of the property being appraised. Evidence for such fees may be established by objective third-party information, such as government agency fee schedules, academic studies, and independent private sector surveys. Fee studies shall exclude assignments ordered by known appraisal management companies.*

However, the results of the Interim Final Rule are clear. The Rule has perpetuated a two-tiered or bifurcated market, where retail appraisal fees float at one level, and those involving AMCs float at a lower level. According to our research, fees to appraisers paid by AMCs are significantly lower than fees paid directly by lenders or through other objective sources such as by the Veteran's Administration according to their VA Fee Schedule. In October, the Appraisal Institute conducted a survey of appraisers regarding the VA Fee Schedule, and the results demonstrate slight to strong majorities of respondents said VA appraisal and inspection fees are "Reasonable" or "Very reasonable"[1]. Further, this research illustrates VA appraisal fees are on par with fees for similar non-VA appraisal and inspection assignments and that when VA appraisal fees are not on par, the fees apparently tend be below par more often than above par.

To illustrate the bifurcated market, we provide a comparison of selected fee schedules for the Veterans Administration and those in the same states of a major AMC.[2] On average, fees through the AMC are roughly $100 less than those paid directly by the VA.[3] One might argue this is the result of volume discounts. However, one must also ask what is being cut from the appraisal process to enable the appraiser to "make up for it in volume." In our view, such an arrangement helps set us up for another crisis in coming years.

We expect representatives of AMCs and banks will try to contend that AMCs are providing services to appraisers in an attempt to justify the forced fee reductions. We firmly disagree. Here, it is worth noting again, that AMCs have a client relationship with lenders, not appraisers. Further, claims that AMCs are providing marketing and invoicing services to appraisers are not accurate. In fact, our members report that some AMCs themselves are among the worst offenders of failing to pay appraisers. Further, appraisers with clientele beyond one AMC still have overhead expenses relating to marketing and accounts payable, so any purported benefit to appraisers is an overstatement, at a minimum.

Also, we expect representatives of AMCs will contend "the market" should be the strongest factor in fee determination. We agree, but here, government policies have stood in the way of appraisers charging market fees. For one, many appraisers lost nearly all of their clientele as the result of the prohibition of orders by mortgage brokers. Prior to 2008, mortgage brokers represented roughly 60 percent of all residential appraisal orders. Today, mortgage brokers are no longer allowed to order appraisals for loans sold on the secondary market. Many banks can manage the appraisal function internally; however, a significant portion of work previously derived from mortgage brokers is now channeled through AMCs.

Further, long standing policies of the Federal Housing Administration (FHA), which were recently corrected but helped to establish the bundled service business model of many AMCs, stood squarely against the notion of allowing the market to run its course. In 1996, FHA approved a policy that effectively capped fees to appraisers. The policy said that if an AMC was used, the consumer could only be charged what was customary and

---

[1] Appraiser Opinions on Department of Veterans Affairs Appraisal and Inspection Fees. Appraisal Institute. October 5, 2010. Available at
http://www.appraisalinstitute.org/newsadvocacy/downloads/key_documents/AI_VA_AppraisalFeeSurveyOct52010.pdf
[2] http://www.appraisalinstitute.org/resources/MD-NY-CA-VA_FeeSchedules.pdf
[3] http://www.appraisalinstitute.org/resources/MD-NY-CA_AMC_FeeSchedule.pdf

reasonable to appraisers in the market area[4]. The policy mistakenly furthered a myth that appraisal and appraisal management functions are one and the same, when they are clearly different[5]. One (appraisal) is a professional service; the other (appraisal management) is a bank administrative function. In essence, the FHA policy that stood for more than a decade allowed lenders to start with what is normally paid to appraisers and work down to carve out an AMC fee. This was not as significant of an issue when AMCs represented less than 20 percent of the market. With the mortgage broker ban and AMC market share now pushing 70 percent, this business model is unsustainable, and it's one of the main drivers behind the inclusion of the customary and reasonable fee requirement by Congress last year.

Recommendation
We urge the CFPB to give appraiser independence and appraisal quality the highest priority by revising the first presumption of compliance to require consideration of direct lender fees to appraisers or fees absent the involvement of AMCs. The CPFB should specify that creditors are required to evaluate appraisal fees that involve non-AMC engagements when undertaking the first presumption, even though the use of a third-party survey is not necessarily required. Such information that segregates appraisal fees paid directly by lenders is readily available in the marketplace – we are aware of at least three private sector sources widely used by lenders that identify fees paid to appraisers absent the involvement of AMCs. The Department of Veterans Affairs fee schedules that are established for various geographic markets are another reliable source. Consideration of this "fee schedule" information, along with other factors such as scope of work and qualifications, would help to alleviate the inconsistencies in the fees that AMCs are allowed to pay under the first presumption and those that are paid under the second presumption.

B. Consumers should understand all charges assessed, including appraisal management

Real estate agents have reported that consumers are paying higher appraisal fees in recent years[6], yet according to our members, appraiser fees have declined by as much as 40 percent[7].

How can this be the case? The answer is simple – lenders have passed through appraisal administration expenses onto the backs of consumers through the Appraisal line of the HUD-1.

Current RESPA interpretations allow for, and even promote, "bundled" fees to consumers, whereby appraisal management fees are lumped together with actual appraisal fees. When a lender utilizes an AMC, HUD's current interpretation of RESPA dictates the fee paid to the AMC – not the actual appraiser – be disclosed to the consumer on Truth and Lending disclosures and listed on the HUD-1 settlement statement[8]. As a result, a perverse incentive exists for AMCs to seek reductions in appraisal fees to carve out larger profit margins.

---

[4] From FHA Mortgagee Letter 97-46, available at http://portal.hud.gov/hudportal/documents/huddoc?id=DOC_14644.txt
[5] FHA "correct" ML 97-46 by issuing Mortgagee Letter 09-28, available http://www.appraisal.state.az.us/userfiles/file/09%2009%20FHA%20Mortgagee%20Letter%202009-28.pdf
[6] From NAR survey, available at http://www.docstoc.com/docs/9041271/NAR-HVCC-appraisal-survey-results
[7] "Impact of AMCs – Member Survey." Appraisal Institute, May 25, 2009.
[8] "**Q:** If an appraisal is ordered through XYZ appraisal vendor management company and the appraisal is subcontracted to ABC Appraisal Company, what name is identified in Line 804 on the HUD-1?

It is also a misrepresentation of our profession.

We believe this policy should be reexamined. Moreover, the CFPB, that will soon have responsibility over these matters, should clearly disclose to consumers how much and which company or individual is being paid for the appraisal. **After all, it is the consumer who pays these fees in nearly all transactions.**

We are not aware of any value to the consumer in a bank using the services of an AMC. The benefit is clearly and solely to the bank, who is passing through a traditional overhead expense on to the backs of consumers. What is particularly troubling to our organizations about the current interpretation of RESPA is that it enables AMCs to operate virtually in the dark. Consumers are led to believe the "Appraisal Fee" being paid to a creditor is for a property appraisal, when in fact it could be for the appraisal as well as appraisal management services. In talking with chief appraisers of banks and financial institutions about this situation, we understand most AMCs actually refuse to disclose the portion of the appraisal fee they have taken for themselves, even upon request by their lender-clients. In essence, the AMCs take from the pockets of appraisers every time an appraisal is completed by an appraiser for an AMC and nobody knows how much. This is not solely the fault of the AMCs but also creditors who seek to outsource their valuation needs to AMCs, but only offer AMC's the same fee, or something similar, previously paid for appraisal services only.

As such, a requirement that the consumer shall not pay for the services of the AMC would possibly solve the customary and reasonable fee debate in its entirety. Such a policy if enacted by the CFPB would facilitate enhanced competition between the outsourced AMC model and the internal appraisal department model, giving banks the option of choosing between using (and paying for) the services of an AMC or performing similar services internally. We believe an alternative arrangement that recognizes and establishes two markets – one for appraisers, and one from AMCs – would deleverage the AMCs from the fee process and enable each market to act on their own. Further, requiring the creditor to pay each separately would allow AMCs to compete for the management services provided to lenders based on *service*, and not nearly exclusively on *price*, such as the case today. Lastly, we believe this arrangement would be consistent with the spirit of the Federal Housing Administration's Mortgagee Letter on this subject (ML 09-28) which requires that FHA Roster appraisers be compensated at a rate that is customary and reasonable for appraisal services performed in the market area where the services are being performed. ML 09-28 also requires that AMC fees not exceed what is customary and reasonable for such services provided in the market area of the property being appraised[9].

The CFPB is well positioned to prohibit consumer payment of appraisal management services under the perspectives stated above. We note the CFPB has been granted authority over TILA and RESPA and that the Dodd-Frank Act authorizes separation of appraisal management and appraisal services on the HUD-1 settlement statement. However, we are disappointed to see the CFPB has carried forward the status quo in the first drafts of the revised Good Faith Estimate. All drafts released to date fail to separate the estimated fees to the appraisal and those estimated for appraisal management.

A: XYZ appraisal management company must be identified on Line 804." From "New RESPA Rule FAQs," April 2, 2010. Available at http://www.hud.gov/offices/hsg/rmra/res/resparulefaqs422010.pdf

[9] From Mortgagee Letter 09-28, issued September 18, 2009. Available at http://www.hud.gov/offices/adm/hudclips/letters/mortgagee/files/09-28ml.pdf

Moving forward, another issue will likely need to be resolved. The Dodd-Frank Act authorizes the separation of AMC and appraisal fees on the HUD-1, however a separate provision (known as the "Merkley amendment") complicates the issue greatly by imposing a 3 percent cap on points and fees relating to the loan. Some banks own AMCs as affiliates. If the fees paid to these entities are separated from the appraisal fee as authorized under Dodd-Frank, it would subject capitively-owned AMC fees to the 3 percent points and fees cap as an affiliate of the bank. This would place such AMCs at a competitive disadvantage in the marketplace.

To address this issue, and to implement the authorization for separation of AMC and appraisal fees, we strongly support separation of AMC and appraisal fees on all consumer mortgage disclosure documents, including the GFE and HUD-1. Further, we believe the CFPB should exempt AMC fees from the points and fees cap, as authorized by the Dodd-Frank Act.

C. Appraisers should be allowed to analyze all sales in a market, and their judgment and expertise should be respected

In 2011, four bills were introduced in state legislatures (Illinois, Maryland, Missouri, and Nevada), and one bill was introduced in Congress and referred to this Committee, to inappropriately legislate the appraisal process. Each proposal would prohibit the use of distressed sales, such as foreclosure sales or short sales, as comparables in an appraisal of a parcel of real property. While we sympathize with the plight of those in today's real estate market, we strongly oppose such bills, for they will only contribute to an asset bubble and place lenders at great risk.

It seems reasonable to assume that distressed sales should not form the basis for market value opinions. But, in some markets, they are such heavy weights on value that they must be considered along with appropriate adjustments. Distressed sales such as foreclosure sales and short sales are common in a declining market. Depending on the severity of the local market downturn, some, many, or even all sales that occur do so under distressed conditions. Appraisers cannot categorically discount foreclosures and short sales as potential comparable data in the sales comparison approach. However, due to differences between their conditions of sale and the conditions outlined in the market value definition they might not be usable as market information. Foreclosures and short sales usually do not meet the conditions outlined in the definition of market value. A short sale or a sale of a property that occurred prior to a foreclosure might have involved atypical seller motivations (e.g., a highly motivated seller). A sale of a bank-owned property might have involved typical motivations, so the fact that it was a foreclosed property would not render it ineligible as meaningful comparable data that should be considered in developing a credible appraisal. However, if the foreclosed property was sold without a typical marketing program, or if it had become stigmatized as a foreclosure, it might need to be adjusted if used as comparable evidence of value. Further, some foreclosed properties are in inferior condition, so adjustments for physical condition may be needed.

As is always the case in selecting sales to use as comparable market information, appraisers must investigate the circumstances of each transaction, including whether atypical motivations or sales concessions were involved, the property was exposed on the market for a typical amount of time, the marketing program was typical, or whether the property condition was compromised. Adjustments might need to be made for these circumstances. When it is necessary to use a distressed sale as evidence of value, the appraiser must carefully analyze the current local market to determine if an adjustment for conditions of sale is needed. If no adjustment is warranted, the lack of adjustment should be explained.

Physical condition and conditions of sale are two distinctly different factors that must be considered separately. They may be related to some degree in a distressed market, but not necessarily. An appraiser must not assume, for example, that a property was in inferior condition simply because it was a foreclosure. The level of investigation needed to meet the requirement for sufficient diligence is generally more than is needed in non-distressed market situations. Further, supporting such adjustments can be particularly challenging when there are few current transactions to analyze. Competency in performing such investigation and analysis is essential, which is why we believe the best and most productive way to alleviate concerns about appraisals in complex markets is to ensure that highly qualified appraisers– particularly those with advanced training, peer review, and competency exams – are used by lenders and their agents.

Further, under federal and state law, appraisers are required to follow the Uniform Standards of Professional Appraisal Practice (USPAP). USPAP Standards Rule 1-4(a) requires that appraisers "must analyze such comparable sales data as are available." This means all sales, including foreclosures and short sales. In some markets, there are so many distressed sales that they are the market and must be considered. When there is a glut of distress sales in the marketplace, and those properties are truly comparable to the subject, it would be misleading not to use them as part (or in some cases all) of the basis for a value conclusion.

USPAP further states that, "When compliance with USPAP is required by Federal law or regulation, no part of USPAP can be voided by a law or regulation of a state or local jurisdiction."

As such, we urge that this Committee refrain from legislating the appraisal process and refrain from advancing the appraisal provisions of H.R. 1755, as introduced.

D. We must focus on the *service provider*, not just the *service*

To its credit, one thing the Home Valuation Code of Conduct did well was reduce "value pressure" on appraisers, meaning, pressure to provide predetermined values has decreased substantially according to our members. However, in doing so, the HVCC, and the resulting repurchase risk, has created a host of problems for appraisers and lenders. These include:

a. "Scope creep" by underwriters and lenders, or subtle increases in scope of work as a result of proprietary rules established simply to paper a file, while fees dictated to appraisers prevent additional billing for the additional work. Automated quality control and assurance systems that are mistakenly read to be appraiser performance measures, rather than property or market risk indicators.
b. Further commoditization of the appraisal process, whereby appraiser-to-appraiser conversations are rare, as interactions with lender or AMC staff, many of whom have little or no knowledge of the appraisal process, much less recognized methods and techniques, multiplies.

Arbitrary rules, such as adding additional comparable sales that provide little credibility to the appraisal, are now commonly requested by underwriters and lenders. Such requests are often made well after delivery of the appraisal report and are tied directly to internal or proprietary rules established to provide protection from repurchase risk. Some automated compliance review systems ordered by lenders virtually never clear an appraisal without raising a red flag on one or many issues. If no appraisals are passing such a system, it begs the question of what purpose such systems are actually performing.

What is striking about such systems is the lack of attention paid on the service *provider*. It is our view that if lenders paid as much attention to the credentials of the appraiser (or the individuals performing the appraisal) as they do to critiquing the form or end product, many of their problems would be solved. However, rare is the day in consumer mortgage appraisal engagement when lenders or their agents ask whether the appraiser is professionally designated by a professional appraisal organization, or has both market and geographic competency to conduct the appraisal assignment. Instead, impersonal and/or automated systems that attempt to protect lenders through quantity (and price) rather than quality are the norm.

Unfortunately, these problems may be exacerbated by the Uniform Appraisal Dataset (UAD) planned to be implemented by Fannie Mae and Freddie Mac this fall. This initiative has been characterized by some as an advancement or improvement to appraisal quality. While the UAD will result in a standardization of data collected by Fannie Mae and Freddie Mac, it may not necessarily result in improved appraisal quality. In fact, in may result in further masking the work of less than competent appraisers, who provide "good looking" data that is poor in quality. The reason for this is simple – data standardization does not magically convert poor data and weak analysis into quality data and professional analysis. Form processing software, which can produce an attractive report, is currently available. But, especially as we have seen in recent years, report appearance has been mistaken for professionalism. As our members have reviewed UAD, they have informed us that it has the potential to further mask the poor quality opinions delivered in high quality reporting.

Credible real estate appraisal requires independent appraisers and competent analysis, which in many cases is best provided in a thoughtfully composed *narrative* format. While there may be examples of where the new descriptors may be better at identifying characteristics and issues than merely marking "x" or "average" as we have now, disallowing certain data from the form forces the appraiser to place additional information in the addenda. In some cases, it's simply unwise to even attempt standardization because it creates potential conflicts with the Uniform Standards of Professional Appraisal Practice (USPAP). In this regard, it is worth noting that the Appraisal Standards Board and state appraiser regulatory agencies have expressed concern regarding the enforcement of UAD appraisals and for consumers and lenders to be misled by UAD reports.

It is also worth noting the original UAD project intended to standardize only a handful of fields with appraisal reports. However, as data systems analysts became involved with the project, UAD morphed into what appears to be a gigantic data mining project. Quite literally, the UAD is now attempting to standardize every significant element and field within commonly used residential appraisal forms. Uniform appraisal standards, state licensing requirements, and the integrity of the appraisal process will require appraisers to add a multitude of addendums to appraisal reports to comply with USPAP and state licensing requirements. This will increase the scope of work for appraisers and increase costs for lenders and consumers. Appraisal costs are directly proportional to the appraisal scope of work and the time expended on the assignment. As such, there is a strong chance that UAD will actually increase the time/effort expended and, as a result, the cost of appraisals

Standardization of data may assist the GSEs in analytics. But it seems reasonable that the GSE's would desire a higher level of professional analysis to provide this more robust data. If the market will not accept increased appraiser fees, professional appraisers will continue to abandon mortgage lending work in favor of alternate assignments, leaving GSE-related assignments to less capable practitioners.

Part II: Public Accountability and Regulatory Oversight of Appraisal Functions

A. Appraiser regulators must be held accountable and observe their Congressional authorizations.

We are deeply concerned about recent actions taken by the Appraisal Subcommittee (ASC) that raise serious questions about its oversight capabilities. Evidence suggests the ASC has asserted inappropriate influence, or direction, to The Appraisal Foundation (TAF), beyond its authorization from Congress. Instead of monitoring and reviewing TAF, the ASC appears to have made TAF an arm of the ASC and is in effect directing some of its activities.

Specifically, the ASC, as a significant financial underwriter of TAF activities, appears to have directed TAF to establish an "Appraisal Practices Board" with the intent to deliver federal funding prior to authorization by Congress. Such actions would far exceed the ASC's statutory mandate and would have the intended effect of usurping Congress' role in establishing law and policy.

We urge Congress not to let these actions go unchallenged. In fact, we believe it may be incumbent upon Congress to establish legislative protocols relative to the relationship between the ASC and TAF. Last, as the mission and role of TAF changes, so too should its Congressional authorization, as it is wholly appropriate for Congress to establish boundaries and parameters to entities receiving public funds.

For background, TAF is a not-for-profit organization recognized by Congress[10] to perform certain limited functions relating to appraisal standards and appraiser qualifications. TAF was mandated with promulgating the Uniform Standards of Professional Appraisal Practice (USPAP) for federally related transactions, as well as issuing the minimum qualification criteria for appraiser certification and licensure. Both the Appraisal Standards Board (ASB) and Appraiser Qualifications Board (AQB) are designed to be independent of TAF's Board of Trustees in carrying out their duties.

Section 1103(b) of Title XI of FIRREA authorizes the ASC, along with monitoring state licensing agencies, to "monitor and review the practices, procedures, activities, and organizational structure of TAF.[11]" on behalf of the federal financial regulatory agencies. The ASC is charged with reporting to Congress on these activities each year. While the ASC attends or observes meetings of TAF, and reviews and approves funding requests relating to appraisal standards and appraiser qualifications, it *does not* have the ability to "direct or overrule specific actions" of TAF. According to a September 11, 2002 letter from the ASC:

---

[10] 12 U.S.C. 3331-3351, available at https://www.asc.gov/Documents/TitleXI/TitleXI.pdf
[11] 12 U.S.C. 3332, available at https://www.asc.gov/Documents/TitleXI/TitleXI.pdf

> *Title XI does mandate that the ASC 'monitor and review the practices, procedures, activities, and organizational structure of the Appraisal Foundation' and the AQB, Congress did not provide the ASC with the authority or the power to direct or overrule the operations or structure of these private entities."* [12]

Currently, the ASC is authorized to provide grants to TAF in support of Title XI responsibilities related to appraiser qualifications and appraisal standards. No direct Congressional authorization exists to provide grant funding in the area of "best practices," or recognized methods and techniques. "Standards" are guiding principles, and they are "standard," meaning their application does not change much, if at all, with the situation. "Best practices" are fluid; what they are and how they are applied is highly dependent on the specific circumstances.

ASC/TAF Efforts to Codify Best Practices

Despite these limitations, for approximately the past two and one-half years, the ASC or its influential member(s) presided over a campaign to establish a new TAF board, known as the "Appraisal Practices Board" or APB. The ASC first expressed its aspiration to expand TAF's mission beyond standards and qualifications in the December 2008 monthly meeting of the ASC[13]. At this meeting, two ASC members, one of whom was the chair, expressed a desire for TAF to address appraisal methodology or practice issues.

It is unfortunate that members of the ASC committed to advance such an endeavor, knowing that Title XI limited TAF to the areas of standards and qualifications, and despite TAF's acknowledgement that such an endeavor would be "encroaching" on other organizations"[14]. The body of knowledge and education on methods and procedures has been long reserved to academia and the professional appraisal organizations.

It should be noted that during this period of time, the ASC was without an executive director for nearly two years, so greater responsibilities and authorities were placed in the hands of the members of the ASC, particularly the chair. This was also a period in which the ASC faced sharp public criticism over its effectiveness in handling appraisal oversight[15].

To address what the ASC and TAF perceived as a shortcoming in appraisal practices, both organizations jointly advanced an amendment in the House Financial Services Committee in May 2009 to a prior version of H.R. 4173. Specifically, the amendment would have required all appraisals of federally related transactions to be prepared in accordance with "best practices" or "recognized methods and techniques" developed or recognized by the

---

[12] From Appraisal Subcommittee correspondence with George R. Harrison, Ph.D., September 11, 2002, available at https://www.asc.gov/documents/othercorrespondence/ltr%20harrison%20request%2009.11.02.pdf

[13] From the ASC Meeting Minutes, December 2008, https://www.asc.gov/Documents/MeetingMinutes/ASC%20Bd%20Mtg%20Minutes%2012.11.2008.pdf

[15] Weiss, M. (2008) October 28. "Appraisal agency's new chief quits after first day." *Associated Press.* Available at http://www.blueridgenow.com/article/20081028/NEWS/810280277/1170

[16] From Appraisal Foundation Letter to the Subcommittee on Capital Markets. April 22, 2009. Available at http://www.appraisalinstitute.org/newsadvocacy/downloads/TAFbestpracticesproposal.pdf

[15] Weiss, M. (2008) October 28. "Appraisal agency's new chief quits after first day." *Associated Press.* Available at http://www.blueridgenow.com/article/20081028/NEWS/810280277/1170

[16] From Appraisal Foundation Letter to the Subcommittee on Capital Markets. April 22, 2009. Available at http://www.appraisalinstitute.org/newsadvocacy/downloads/TAFbestpracticesproposal.pdf

Appraisal Foundation.[16] This amendment would have authorized federal funding to TAF in the area of appraisal practice, methodology and, potentially, appraisal instruction, without further clarification.

Representatives of both organizations lobbied leaders of the Appraisal Institute in a private meeting to support the amendment. Ultimately, the amendment was never considered by the Committee and was not included in the final version of H.R. 4173 due to concerns about its merits and enforceability.

However, failure to secure Congressional authorization to expand TAF's authority to the area of appraisal practices did not impede the ASC and TAF from advancing the project. A special "Best Practices Task Force" had been convened by TAF to examine the issues of appraisal methodology and best practices. The formation of the Task Force occurred concurrently with the development of the legislative amendment advanced by the ASC and TAF, although the existence of the amendment was apparently never disclosed to Task Force participants, and the bulk of the Task Force's work occurred after the amendment was rejected by the House Financial Services Committee.

Our organization was, and remains, deeply concerned about the functions and operations of this Task Force, especially after the ASC's and TAF's overtures on appraisal methodologies and techniques were rebuffed by Congress. Members of the ASC were originally a part of this Task Force and may have instrumental in its creation. However, legal counsel from the respective federal financial institution regulatory agencies apparently removed the ASC members shortly after the Task Force convened because of concerns about conflicts of interest.

The Final Report of the Task Force on Best Practices does not appear to be consistent with the Task Force's actual deliberations[17]. For instance, we understand from participants of Task Force meetings that leaders of TAF spoke openly about developing appraisal education and future revenue opportunities as a result of the creation of a panel or committee relating to appraisal methodology and instruction. Concerns were expressed by several members of the Task Force about the mission creep of TAF, the scope and enforceability of the project, and the potential conflicts of interest. Yet, the Report includes only a scant mention about potential conflicts, and it relates more to potential overlap with other TAF boards. It omits any concerns expressed by Task Force members about education development. This leaves us to speculate that the recommendations of the Task Force may have been predetermined by the ASC and TAF, and that creation of the Task Force was only to give the illusion of objectivity and openness. Further, it appears that federal funds provided by the ASC were used by TAF to reimburse expenses relating to the Best Practices Task Force, a questionable reimbursement given Title XI's limitations.[18]

Despite repeated concerns and reservations expressed by our organization and others, representatives of TAF proceeded to present a funding request to the ASC in September 2009 for monies to support funding a panel – called the Recognized Methods and Techniques Panel (RMAT) - recommended in the Report of the Task Force

[16] From Appraisal Foundation Letter to the Subcommittee on Capital Markets. April 22, 2009. Available at http://www.appraisalinstitute.org/newsadvocacy/downloads/TAFbestpracticesproposal.pdf
[17] From the Task Force Report to the Board of Trustees, September 11, 2009, available at http://www.appraisalinstitute.org/newsadvocacy/downloads/TaskForceMemo_BOT_091109.pdf
[18] From the ASC Meeting Minutes, September 23, 2009. Available at https://www.asc.gov/Documents/MeetingMinutes/ASC%20Bd%20Mtg%20Minutes%2009.23.2009.pdf

on Best Practices.[19]. This funding request was subsequently withdrawn in November, 2009[20]. The reason for this withdrawal is not entirely clear, but during this period of time the scope of the RMAT project was substantially expanded by the TAF Board of Trustees. While the Task Force recommended creation of a panel, the leadership of TAF disregarded this recommendation and established a third board (the APB) instead.[21]

When leaders of our organization in the fall of 2009 asked TAF leadership why the third board had been created, TAF leadership confirmed they were "told to do it" by representatives of the ASC. The chair of TAF, in a recent interview, confirmed that TAF was "asked by the Appraisal Subcommittee to do this, not informally....[22]" If this position of the ASC is in fact true, it would certainly be well beyond its authorization by Congress, albeit consistent with past actions that would suggest TAF is under direction by the ASC, or at least certain members of the ASC.

The only public accountability requirement of the ASC is to issue an annual report to Congress, which includes a review of the TAF's activities. Remarkably, neither the 2009 or 2010 Annual Reports issued by the ASC divulge any of these activities, reporting only that TAF established the APB and summarizing its intentions, but advising nothing about the apparent influence, involvement and direction advanced by members of the ASC.[23] These reports also fail to mention the expression of concern by the Appraisal Institute regarding this unauthorized mission creep, which ultimately led to AI withdrawing as a TAF sponsor.

Potential Explanations

The original intent behind establishing a third board appears to be to position TAF to receive additional federal funding from the ASC. TAF revenues have declined substantially in recent years, so new funding streams have been sought to help offset recent losses. We see two possibilities for this to occur: 1) direct funding/ reimbursement for its operations, and 2) recognizing future work products of the APB – so-called "monographs" – within ASC regulations and regulations of the federal bank regulatory agencies. TAF leadership openly has expressed their desire to seek federal funding for the APB, having originally sought ASC funding in September 2009. TAF leadership has also implied that federal funding of the APB may follow a similar course as that of the ASB and AQB, which were created prior to Congressional authorization in Title XI[24].

---

[19] From the ASC Meeting Minutes, September 23, 2009. Available at https://www.asc.gov/Documents/MeetingMinutes/ASC%20Bd%20Mtg%20Minutes%2009.23.2009.pdf

[20] From the ASC Meeting Minutes, November 18, 2009. Available at https://www.asc.gov/Documents/MeetingMinutes/ASC%20Bd%20Mtg%20Minutes%2011.18.2009.pdf

[21] From the June 3, 2009 Memo from the TAF Board of Trustees entitled, "Proposed Legislative Amendment/Best Practices."

[22] "*The Appraisal Practices Board is a good example*...we were asked by the Appraisal Subcommittee to do this, not informally [sic], but its members expressed an interest in the Foundation doing this at least." From *"The Housing Helix" podcast with Jonathan Miller, September 15, 2010.* Available at http://matrix.millersamuel.com/?p=9541

[23] From the 2009 Annual Report of the Appraisal Subcommittee. Available at https://www.asc.gov/Documents/AnnualReports/2009%20ASC%20Annual%20Report.pdf

[24] Presentation by David Bunton, President of the Appraisal Foundation before the Association of Appraiser Regulatory Officials, May 1, 2010.

Testimony of Appraisal Institute President-Elect Sara Stephens, MAI, CRE
July 13, 2011

Our organization is troubled by the possibility of the appraisal profession's exclusive standards and qualifications setter being at the mercy of federal bank regulators. On this point, we strongly believe that the public is best served by an appraisal profession that is independent of government control and influence. This important separation of functions was recognized and established by Title XI when it mandated that there be requirements for certification and licensing for real estate appraisers, as well as adherence to USPAP, and reserved the promulgation and issuance of appraisal standards and appraiser qualifications to TAF. This was done with an explicit understanding that the "body of knowledge" of the profession is separate and distinct from standards and qualifications and requires greater flexibility given the diversity of property types and the continuous evolution of valuation theory. It is for this reason that areas of appraisal practice have been reserved to academia, as well as the appraisal practitioners collectively and professional appraisal organizations that have a nearly 80-year history in development of the body of valuation knowledge.

Any directive by the ASC and its members to establish a new board – without Congressional authorization – would go far beyond the ASC's legal mandate to monitor and review activities of TAF related to standards and qualifications as authorized under Title XI. Our organization is not aware of the ASC advising Congress of any concerns regarding areas of appraisal practice and recognized methods and techniques, as well as any perceived disconnect between appraisal standards and appraisal practice. Expression of such concerns in the ASC's Annual Report or in other forms of correspondence would have been an appropriate expression of the ASC's monitoring and review authorization, and yet none can be found in any public Report to Congress[25].

Further, this abrogation of the ASC's oversight responsibility comes amidst growing concerns over the independence of the TAF boards. Specifically, we have heard concerns from several former members of the Appraisal Standards Board (ASB) regarding the independence of the ASB which may have been compromised by TAF's Board of Trustees in recent years. According to TAF By-Laws, the ASB is to operate independent from the TAF's Board of Trustees with regard to the terms and content of USPAP.[26] Former members of the ASB report that members of TAF's Board of Trustees interfered with the ASB's duties and obligations, directing it to take certain actions or avoid taking others. It is this type of activity that Congress trusted the ASC with monitoring; yet, it appears that this oversight function may have been ignored in lieu of the ASC providing direction to TAF.

We also have concerns about the TAF board appointment process and recommend an examination into whether the appointment process to the ASB and AQB is impartial and not subject to personal interests or favors. Specifically, in this regard, the TAF President apparently has considerable influence, and in several cases, we do not believe the better-qualified candidates have been selected. At a minimum, TAF's selection process and criteria should be examined, as should the question of whether or not they have been adhered to. This is an oversight task that the ASC should have performed, but apparently has not.

---

[25] ASC Annual Reports are available at https://www.asc.gov/About-the-ASC/AnnualReports.aspx

[26] *"Except as otherwise provided in these Bylaws or by resolution of the Board of Trustees, the Standards Board shall have and exercise all authority and power and perform all functions of the Foundation and the Board of Trustees in respect to establishing improving and promulgating the terms and content of the Uniform Standards of Professional Appraisal Practice." Available at https://appraisalfoundation.sharefile.com/d-scb075c284704f3c8*

Recommendations
These issues speak to broader concerns that our organization has regarding the overall oversight process outlined by Title XI of FIRREA. The Dodd-Frank Act represents the first significant legislative review by Congress of the ASC in nearly twenty years. While our organization has expressed concerns about the effectiveness of the ASC in monitoring standards and qualifications for many years, the current "review every 20 years approach" is not conducive to active and effective oversight by Congress. We hope Congress will examine this issue and instill much-needed accountability for the betterment of our profession and the protection of the public.

To this end, we question whether the current structure of the ASC includes appropriate oversight and public-accountability measures to protect the public and whether comprehensive reorganization is necessary to accomplish this goal. More specifically, the concerns outlined above illustrate several of the problems with the underlying ASC structure, which appears to allow individual appraisal policy managers in federal bank regulatory agencies to wear two "hats" in the realm of appraisal regulation. Traditionally, the same individuals that write appraisal related policy and guidance for federally regulated financial institutions have been assigned as members of the ASC. These are two entirely different functions, requiring separate and distinct knowledge sets. For instance, it is possible that the directive from members of the ASC to create the APB was based on their experiences as appraisal policy managers at their respective agencies. The appraisal policy managers may have identified problems found in appraisals during bank examinations, and then carried those perspectives to meetings of the ASC. However, the ASC, as illustrated above, is limited by law to monitoring and reviewing the activities of TAF and is prohibited from providing directives. Yet, it may not be clear which hat is being worn – the member of the ASC, or the policy manager of the federal bank regulatory agency.

In addition, as Congress reviews legislative recommendations, we urge its authorizations to TAF be reflective of any change in its mission statement. For instance, we do not believe it would be appropriate for Congress to continue federal funding to TAF if it moves to become a membership organization. We do not believe it is appropriate to continue federal funding if TAF moves to provide education, either directly or indirectly, to appraisers. We see enormous conflicts of interest with exclusive standards-setting bodies also providing education, especially, when that organization *approves* education[27]. Most, if not all, standards-setters that we are familiar with go to great lengths to safeguard their independence by explicitly *restricting or limiting* their involvement in education. In our view, this actually strengthens a standards-body position as an authoritative voice on standards issues by protecting it from any perception of ulterior motives.

TAF was never envisioned by Congress or its sponsors to function like a professional organization and compete with professional organizations. Yet this clearly appears to be part of the intention of the ASC with its directives and TAF with its actions.[28]

This is particularly important in light of the new APB, for which, as recent history has shown, the ASC and TAF will continue to advance and potentially propose again to Congress once it is fully operational. On this point, we do not believe Congress should recognize the APB without establishing appropriate limitations on TAF, including

[27] TAF's Course Approval Program is recognized by state appraiser regulatory agencies and is now recognized in the Dodd-Frank Act. Available at https://appraisalfoundation.sharefile.com/d-s29a914a06494fcc8
[28] A the October 2010 AARO-TAF-ASC meeting in Washington, DC, the President of TAF announced the development of education for real estate appraisers in the area of financial reporting.

restrictions in offering education where there are apparent conflicts of interest. Similar standards-setting bodies and those with authorizations from Congress, such as the Conference of State Bank Supervisors who are authorized by Congress with approving education, are strictly prohibited by Congress from offering education to licensees.[29] We believe such limitations are appropriate for TAF given its role as an exclusive standards-setter, where independence is crucial to protecting the public.

B. Risk management functions must be enhanced with competent and independent appraisers and appraisal reviewers

One of the biggest challenges facing real estate appraisal is the marginalization of risk management processes within many financial institutions. As several recent investigations into the financial crisis have confirmed, bank regulators have failed to properly oversee financial institutions. In some cases, virtually no oversight existed, and it should come as no surprise that many of those institutions are no longer in existence.

In March, 2011, the Federal Deposit Insurance Corporation filed a civil complaint against executives of Washington Mutual (WaMu), illustrating how risk management was marginalized. According to the complaint[30], senior bank executives knew that strong risk analysis and management was critical to managing this type of higher risk loan portfolio. Nevertheless, just at the point when risk management was most critical, the executives allegedly marginalized the risk management function in WaMu's Home Loans Division. Repeated warnings about the risks associated with the bank's aggressive lending practices – even those as stark as senior risk managers declaring that WaMu was "putting borrowers into homes that they simply cannot afford" – went unheeded. As the Bank's chief risk officer told the chief executive just weeks before WaMu went into receivership, the bank's "DNA" was missing "the risk chromosome."

Also in March, the Senate Government Affairs Permanent Investigations Subcommittee issued a report on the failure of WaMu, citing a slew of factors involved. Passive oversight of bank appraisal functions was one of many indictments identified in the report. During the five-year period from 2004 through 2008 reviewed by the Subcommittee, Office of Thrift Supervision (OTS) examiners identified over 500 serious deficiencies in Washington Mutual's lending, risk management, and appraisal practices. With regard to appraisal oversight, the report found the OTS failed to take appropriate enforcement action involves WaMu's appraisal practices. OTS failed to act even after other government entities accused WaMu of systematically inflating property values to justify larger and more risky home loans. Specifically, WaMu's decision to outsource the appraisal function received minimal attention from OTS. Problems began almost immediately after WaMu outsourced the appraisal function.

---

[29] The SAFE Act limits the National Mortgage Licensing System established by the CSBS from directly or indirectly offering education for qualifying or continuing education for mortgage originators. See 12 U.S.C. 5104(c)(3) http://www.law.cornell.edu/uscode/html/uscode12/usc_sec_12_00005104----000-.html. For this reason, the CSBS is not found amongst the list of approved education providers found http://mortgage.nationwidelicensingsystem.org/courseprovider/Documents/NMLS%20Approved%20Course%20Providers.pdf

[30] Available at http://graphics8.nytimes.com/packages/pdf/business/conformedcomplaint.pdf

Similar findings can be found in recent Material Loss Reports, which are conducted by offices of inspectors general following a bank failure. This includes the IndyMac Bank failure, where appraisal citations were found, but not acted on, by bank regulators for many years all the way up until failure. We recently conducted a review of Material Loss Reports and found that 64 percent of Material Loss Reports contained previous citations by bank regulators relating to appraisal management deficiencies in 2009. This percentage increased to 75 percent in Material Loss Reports published in 2010, where failed banks were previously cited for appraisal management deficiencies.

All of these reports indicate the federal bank regulators must become more proficient in appraisal matters. Following the Savings and Loan Crisis of the 1980s, the Office of Thrift Supervision and the Federal Deposit Insurance Incorporation had large appraisal divisions that assisted with bank oversight and supervision. Over time, these divisions were downsized out of existence. At one point in the past decade, there were no appraisers on staff at any bank regulatory headquarters agency. Regulators relied on the expertise from non-appraisers to assist with appraisal oversight and examination issues. Sadly, the results were disastrous.

Today, we are aware of four designated members of the Appraisal Institute who work for bank regulatory agencies, three of whom were hired in the last three years. The Federal Reserve and National Credit Union Administration still do not have any appraisal staff. We understand the Consumer Financial Protection Bureau may assign one staff position for an appraiser, which will be important to oversight of non-bank mortgage lender appraisal and risk management operations. We hope this hiring trend continues, but in a bolder way" or "more robust manner" in order to use the wealth of appraisal knowledge and experience that is available.

Concluding Remarks

If we have learned anything during this crisis it is that we need a return to the basics. We need to reinsert ethics, competency and accountability into the real estate sector. We also need to ensure regulators are doing their job. To this end, it is critical that Congress remain engaged on these matters, as continuing threats continue to loom large over the financial recovery.

RESPRO®
Real Estate Services Providers Council, Inc.

Written Statement

Of

Tim Wilson
President of Affiliated Businesses
Long and Foster Companies

On Behalf of

The Real Estate Services Providers Council, Inc. (RESPRO®)

Before the
U.S. House of Representatives

Subcommittee on Insurance, Housing and Community Opportunity
Of the
Committee on Financial Services

On

"Mortgage Origination:
The Impact of Recent Changes on Homeowners and Businesses"

July 13, 2011

Good morning, Chairwoman Biggert, Ranking Member Gutierrez, and Members of the Subcommittee. My name is Tim Wilson and I am President of Affiliated Businesses for Long and Foster Companies and 2011 Chairman of the Real Estate Services Providers Council, Inc. (RESPRO®).

Long and Foster Companies is the third largest independent residential real estate brokerage firm in the nation, with 185 residential real estate brokerage offices and 13,000 real estate sales associates that engage in real estate sales and leasing in Virginia, Washington, D.C., Maryland, West Virginia, Delaware, Pennsylvania, North Carolina, and New Jersey.

Long and Foster offers mortgage services through Prosperity Mortgage, a joint venture co-owned by Long and Foster and Wells Fargo Home Mortgage with 311 employees that originated 12,500 residential mortgage loans in 2010. We also operate an independent mortgage banking firm, Walker Jackson Mortgage, with 113 employees in southeastern states from Georgia to North Carolina. Another wholly-owned company, Mid-States Title, runs several joint ventures with 200 employees that issued approximately 30,000 title policies and conducted over 18,000 settlements in 2010. We issued 3,898 homeowners insurance policies in 2010 through Long and Foster Insurance, a wholly-owned insurance agency.

RESPRO® is a national non-profit trade association of almost 200 residential real estate brokerage, mortgage, home building, title, and other settlement service companies that offer diversified services for home buyers through affiliated business arrangements that are regulated at the federal level under the Real Estate Settlement Procedures Act (RESPA).[1]

My testimony today will focus on how the "ability to repay" and risk retention standards in the Dodd-Frank Wall Street Reform Act of 2010 (Dodd-Frank) unnecessarily discriminate against affiliated business arrangements, which we believe would reduce mortgage competition and ultimately increase the cost of mortgage credit in many marketplaces throughout the country.

I. An Overview of Affiliated Businesses in the Home Buying and Financing Industry

Affiliated businesses are not new in the home buying and financing industry. According to the independent real estate research firm REAL *Trends*, Inc., the nation's 500 largest residential real estate brokerage firms closed 150,962 mortgage loans and conducted 358,172 title closings through affiliated companies in 2010.

[1] RESPA and RESPA regulations require any person who refers a home buyer to an affiliated settlement service company to:

- Disclose in writing that it may benefit from the referral.
- Disclose an estimate of market prices for the referred service.
- Advise the consumer that there may be lower prices available and that he/she should shop around
- Obtain a written acknowledgment from the home buyer that he/she has reviewed these disclosures.
- Not require the use of the affiliated service.
- Not pay or receive any referral fees from the affiliated company that are otherwise prohibited under RESPA.

In today's challenging housing market, firms like Long and Foster use our affiliated mortgage, title, and other settlement service companies to help assure that our real customers close on time and move into their new homes as scheduled. Because we own or partially own other companies needed to close the home purchase transaction, we can better ensure that they communicate promptly with each other and therefore resolve any service issues that arise more efficiently than we could with independent companies. Our affiliated businesses also help us reduce the cost of the entire mortgage transaction through cost efficiencies achieved from the sharing of facilities, management, technology, equipment, and marketing expenditures.

Since real estate brokerage firms began to offer mortgage, title, and other settlement services over 25 years ago, there have been several consumer surveys and economic studies to assess their impact on the home buyer. Economic studies over the years have shown that affiliated businesses are competitive in cost,[2] and consumer surveys consistently have shown that consumers who use their real estate brokerage firms' affiliated businesses have a more satisfactory home buying experience.[3]

II. The Potential Discriminatory Impact of Dodd-Frank on Affiliated Businesses

Unfortunately, the "ability to repay" and risk retention standards in Dodd-Frank unnecessarily discriminate against the affiliated business model in a way that we believe will reduce competition and ultimately increase the cost of mortgage credit in many marketplaces throughout the country.

Section 1411 of the Dodd-Frank requires mortgage lenders to determine the borrower's ability to repay the loan based on their compliance with a variety of specified practices. Section 1412 of the Act creates a rebuttable presumption that a mortgage lender has complied with the new ability to repay" standard for "Qualified Mortgages" (QMs), which are mortgages that have characteristics that are less likely to pose repayment or other problems for consumers.

Dodd-Frank also specified that a mortgage is not a QM if the total "points and fees" paid by the consumer in the transaction exceed 3% of the loan amount. The problem for affiliated businesses

[2] A 2008 economic study on the costs of affiliated services vs. unaffiliated services involved an independent analysis of over 2200 HUD-1 Settlement Statements from transactions conducted in nine states (Alabama, Illinois, Maryland, Michigan, Minnesota, North Carolina, Ohio, South Carolina and Virginia) in 2003 and 2005. The study concluded that title premiums and title-related settlement closing charges are not higher when affiliated business arrangements are involved compared to when they are not. "Affiliated Business Arrangements and Their Effects on Residential Real Estate Settlement Costs" (2006), The CapAnalysis Group LLC. The CapAnalysis Study reached the same conclusion as a 1994 study performed by the national economic research firm of Lexecon, Inc., which found that title and title-related services for transactions performed by affiliated title companies in seven states – Florida, Minnesota, Tennessee, Wisconsin, Mississippi, Pennsylvania, and California – were competitive with those provided by unaffiliated title companies. "Economic Analysis of Restrictions on Diversified Real Estate Services Providers", by Lexecon, Inc., January 3, 1995.

[3] In a December 2010 Harris Interactive survey, home buyers said that using affiliates saves them money (78%), makes the home buying process more manageable and efficient (75%), prevent things from "falling through the cracks" (73%), and is more convenient (73%) than using separate services. "One-Stop Shopping Preferences 2010", Harris Interactive and the National Association of Realtors (NAR).

is that Dodd-Frank incorporated, with slight variations, the "points and fees" definition in the Home Owners and Equity Protection Act (HOEPA), which was enacted in 1994 as part of amendments to the Truth in Lending Act (TILA).[4] This definition counts title fees charged by a mortgage lender's affiliated title company towards the 3% threshold, but not fees paid to an independent third party title company -- even if the fees charged by the affiliated title company are no more than or less than the charges made by the unaffiliated third party.[5]

As a result, loans in which a mortgage lender's affiliated title company is used would more likely exceed the 3% threshold under the QM exemption under the "ability to repay" standards and the 5% threshold under HOEPA. It would be much more difficult for us to sell loans in which an affiliated title company is used in the secondary mortgage market, and Dodd-Frank elsewhere gives a consumer a perpetual right (without any time limit) to assert as a defense against the mortgage lender a violation of the "ability to pay" standard in any future action to collect the loan.

This same discrimination against affiliated businesses exists under the Dodd-Frank risk retention standards, which require mortgage lenders to retain 5% of the credit risk of loans that are securitized and sold unless the loan is a "Qualified Residential Mortgage" (QRM). Dodd-Frank directed federal regulators to create a QRM definition that is no broader than the definition of QM under the "ability to repay" standards. In their March 29 proposed rule to implement the Dodd-Frank risk retention standard, federal regulators proposed to use the same "points and fees" calculation that discriminates against mortgage companies with affiliated title businesses.

The total number of affiliated loans that would exceed the 3% threshold under the Dodd-Frank "ability to repay" and risk retention standards would depend on the average cost of mortgage origination and title services in each marketplace. The impact, however, clearly would be most significant for smaller loans that are predominant in low-income to lower-middle income marketplaces, since 3% of a $100,000 loan ($3,000) is more easily reached than 3% of a $300,000 loan ($9,000). At that point, companies with affiliated mortgage and title businesses like Long and Foster would need to discontinue offering title services in conjunction with those loans, discontinue offering mortgage services but continue to offer title services, or withdraw from the market altogether.

While I cannot predict the decision of each company faced with this choice, I believe that there would be legitimate reasons for a company with affiliated mortgage and title companies to choose to discontinue offering mortgages but to continue to offer title and title-related services if

---

[4] The U.S. House of Representatives had previously identified the discriminatory impact of the current HOEPA calculation of points and fees on affiliated businesses and had twice passed legislation correcting the discrimination (the 2007 Mortgage and Predatory Lending Act and the 2010 Dodd-Frank legislation) by exempting affiliated fees or premiums for title examination, title insurance, or similar purposes from the HOEPA points and fees threshold as long as the fees were reasonable and as long as the affiliated company complied with RESPA's affiliated business regulations. This provision of the 2010 House-passed Dodd-Frank legislation was inexplicably removed the Dodd-Frank House-Senate Conference.

[5] Standing alone, HOEPA's "points and fees" definition has a less significant impact on affiliated businesses since Dodd-Frank set the HOEPA threshold at 5% of the loan amount. However, it still would prevent companies like Long & Foster from offering both mortgage and title services on small loans which are most predominant in lower-income areas.

it believes that the cost of both services could exceed 3% of the loan amount. Because of the negative consequences of originating a loan that is not a QM under the Dodd-Frank "ability to repay" standards or a QRM under the risk retention standards, it would be important to have certainty as to which loans would exceed the applicable thresholds. The cost of mortgage origination services is highly dependent on the customer's individual decisions and is more difficult to predict on an aggregate basis, while title fees and premiums are either regulated or filed in the majority of states.

Consequently, if the Dodd-Frank "ability to repay" and risk retention standards take effect as passed, RESPRO® believes that competition for mortgage loans would decrease in many low- and lower-middle income marketplaces predominated by smaller loans because of the withdrawal of affiliated businesses from those marketplaces. Consumers would have fewer choices and the cost of mortgage credit would increase.[6]

III. Congress Should Exclude Affiliated Title Fees from the HOEPA "Points and Fees" Threshold that Was Incorporated in the Dodd-Frank "Ability to Repay" and Risk Retention Standards

RESPRO® believes that Congress can prevent this negative impact on competition and the cost of mortgage credit in the mortgage marketplace by amending the Truth in Lending Act to create a narrow exemption for affiliated fees or premiums for title examination, title insurance, or similar purposes from the 3% HOEPA threshold that was incorporated into the Dodd-Frank "ability to repay" and risk retention standards.

It is our understanding that Congress originally included a variety of affiliated fees in the "points and fees" threshold in HOEPA because of its concern that mortgage companies might attempt to circumvent HOEPA by moving fees to affiliated companies, which would reduce the possibility that a loan would be determined to be a "high cost" loan that was subject to HOEPA.

However, HOEPA already states that any charge that is not "reasonable" must be included in the applicable points and fees threshold, thereby requiring that any affiliated charges must be reasonable in order to be excluded from the threshold. If Congress amends the Truth in Lending Act to create a narrow exemption for affiliated fees or premiums for title examination, title insurance, or similar purposes from the "points and fees" threshold; this requirement would remain. Federal regulators would be able to readily determine if affiliated title fees are "reasonable" because the majority of states require that title insurance rates be set by the state, approved by the state, or filed with the state.[7]

[6] Even if a company chooses to continue offering mortgages but to discontinue offering affiliated title services with loans in which the 3% threshold would be reached, RESPRO® believes that consumers would be harmed because (1) the withdrawal of affiliated title services in a marketplace would create an upward pressure on title fees and premiums; and (2) cost efficiencies from the sharing of facilities, management, technology, equipment, and marketing expenditures among affiliated businesses would be eliminated.

[7] 44 states require that title insurance rates be set by the state, approved by the state, or filed with the state. Of the remaining six states and the District of Columbia, two states (Iowa and West Virginia) do not recognize title insurance and one state requires that the rates be posted. A.M. Best, Report to National Association of Insurance Commissioners (NAIC), 2006. In addition, RESPA prohibits a mortgage lender from requiring a consumer use its affiliated title company, so federal regulators would be able to compare

III. Summary

In summary, we urge Congress to correct the discrimination against mortgage companies with affiliated title businesses in the Dodd-Frank "ability to repay" and risk retention standards that would unnecessarily result in the withdrawal of affiliated mortgage or title services from many marketplaces in the country to the detriment of consumers.

Thank you for the opportunity to testify on behalf of RESPRO®'s members.

---

the costs of loans in which the affiliated title company was used to those in which it was not used by reviewing the closing documents of mortgage lenders with affiliated title companies which would include both affiliated and unaffiliated title costs.

Insurance, Housing and Community Opportunity Subcommittee July 13, 2011 Hearing on "Mortgage Origination: The Impact of Recent Changes on Homeowners and Businesses"

Responses to Additional Questions from Chairman Biggert for Mr. Jim Park, Executive Director, Appraisal Subcommittee[1]

1. The ASC was created in 1989 as part of legislation designed to address problems arising from the 1980s savings and loan crisis, including faulty and fraudulent appraisals. ASC's specific responsibilities include monitoring the activities of state appraiser regulatory agencies; the appraisal requirements of the Federal banking regulators; and the practices, procedures, and activities of The Appraisal Foundation (TAF).

    a. Over the past 10 years, what have been the major impacts of ASC's monitoring efforts? To what extent, if at all, has state compliance with Federal appraisal requirements improved over this period?

Response: In 2005, the ASC increased the frequency of Compliance Reviews from once every three years to once every two years, at a minimum. Increasing the frequency of ASC Compliance Reviews has enabled the ASC to discover State compliance issues earlier, therefore making the corrective process less difficult and time consuming.

The ASC has made an effort to improve its State oversight and monitoring consistent with Title XI of the Financial Institutions Reform, Recovery and Enforcement Act (Title XI). To assist States in carrying out their Title XI-related duties, in 2009 the ASC implemented an improved Compliance Review process to encourage and allow States to correct deficiencies prior to the final ASC Compliance Review Report being issued. The ASC Compliance Review process now provides States the opportunity to review the ASC staff's Preliminary Findings, ask for clarifications and provide their response to the ASC prior to a final determination of compliance. After receiving a State's response, the ASC is presented with staff recommendations that include the State's response. The ASC then makes its determination based on the State's response and the ASC staff recommendations.

State compliance with Title XI has improved since the implementation of the revised Compliance Review process and cycle. During the 2007/2008 Review Cycle, ASC staff reviewed 56 State appraiser regulatory programs (Programs). Of those 56 State Programs, only 9 (16%) were "in substantial compliance"[2] with Title XI. It is important to note that a relatively minor deficiency will result in a Program being found "not in substantial compliance." During the first complete Review Cycle under the new Compliance Review process for 2009/2010, ASC staff reviewed 58 State Programs. Twenty-

[1] The Appraisal Subcommittee, as a matter of policy, disclaims responsibility for any private publication or statement by any of its Subcommittee members, officers, or employees. The views expressed herein are those of the author and do not necessarily reflect the views of the Subcommittee.

[2] "Finding" Defined for ASC Compliance Review Report:

1. In Substantial Compliance: Applies when no issues of non-compliance or violations of Title XI are identified.
2. Not in Substantial Compliance: Applies when there are one or more issues of non-compliance or violations of Title XI, but the concerns do not rise to the level of "not in compliance."
3. Not in Compliance: Applies when the number, seriousness, and/or repetitiveness of the Title XI violations warrant this finding.

An "Area of Concern" is to be used when a specific area is in compliance but could be improved. Areas of Concern may appear within any Report, regardless of the Finding.

three (40%) were found "in substantial compliance" with Title XI. The primary reason for the improved compliance rate is that States are now given the opportunity to correct any deficiencies in their Programs prior to a final finding by the ASC. The ASC believes the new process is leading to improvements in State regulation of appraisers. However, most of the Compliance Review modifications undertaken by the ASC have been in recent years, so there is not sufficient data to draw conclusive results regarding improvements to State regulation as a result of the modifications.

In an effort to support States' efforts to comply with Title XI the ASC has:

- Funded Investigator Training Courses which are administered by the Appraisal Foundation and designed and taught by the Association of Appraiser Regulatory Officials (AARO);
- Participated in the first joint AARO, Appraisal Foundation and ASC conference;
- Participated on a Consistent Enforcement Task Force with the Appraisal Foundation and State appraisal regulatory officials;
- Funded and participated in the development of a filmed mock trial that is now available in the Appraisal Foundation's E-Library for training purposes;
- Funded and participated in developing and presenting a Board Member Training course that is now available in the Appraisal Foundation's E-Library;
- Updated the National Registry to allow States to report appraiser data in real time or by an upload of data directly from the State;
- Issued Bulletins to the States regarding implementation and effective dates of provisions within the Dodd-Frank Act;
- Provided presentations to the National Governors Association to educate Governors' staff on the importance of Title XI;
- Wrote letters to governors and budget officials to support States' need for resources;
- Reviewed and commented on States' proposed statutes and regulations;
- Provided presentations to AARO and other entities concerning ASC activities;
- Updated the ASC website, adding a Resources for State Appraiser Regulatory Agencies with quick links to important sites; and
- Added a website page that assists States regarding what is expected in different areas of the Compliance Review to show compliance with Title XI.

b. How specifically does ASC monitor the appraisal requirements of the Federal banking regulators, and what impact has ASC's monitoring had on appraisal oversight?

Response: Title XI requires the ASC to monitor the requirements established by the Federal financial institutions regulatory agencies with respect to "(A) appraisal standards for federally related transactions under their jurisdiction, and (B) determinations as to which federally related transactions under their jurisdiction require the services of a State certified appraiser and which require the services of a State licensed appraiser." There is no formal process established for the ASC to monitor the appraisal requirements established by the Federal financial institutions regulatory agencies. It has been a long-standing policy of the ASC to include a section on the activities of the regulators and HUD regarding appraisal-related regulations and policy initiatives in the ASC Annual Report.

Further, several of the ASC members represent their agencies on an interagency workgroup being formed to address appraisal-related regulations as required by the Dodd-Frank Act. Those ASC members could provide updates and information on appraisal-related policies to ASC staff and the other ASC members. The

HUD representative to the ASC has also provided updates on HUD appraisal-related policy initiatives with regard to FHA-insured loan programs. According to some ASC members, there are limitations to these discussions with regard to pre-decisional agency matters and agency proposals during a public comment period. The agencies also will seek technical assistance from ASC staff on appraisal practices and standards. For example, ASC staff participated in interagency discussions with Federal Reserve Board staff in the development of amendments to Regulation Z (Truth in Lending) to address certain appraisal provisions in the Dodd-Frank Act related to appraisal independence requirements.

2. ASC is authorized to establish advisory committees, hold hearings, take testimony, receive evidence, provide information, and perform research.

    a. To what extent has ASC exercised this authority?

Response: Though the ASC has never formed Advisory Committees, the ASC has formed various working groups to perform research. For example, in 1995, the ASC established a Registry Team, primarily of ASC staff with input from various States, to examine and make recommendations to the ASC regarding the National Registry. In 1996, the Registry Team completed its review and recommendations regarding the National Registry, including the State data submission process and how the National Registry data is distributed to the States and others. As a result, the National Registry was successfully redesigned and went public on January 1, 1998, on the ASC website. This redesign provided greater public access to the Registry and its contents, including the ability to download the National Registry.

Title XI also required the ASC to complete two studies:

- The ASC completed a study for Congress on whether comparable sales and financing information is both sufficient and available to appraisers to enable them to properly estimate the value of property in connection with federally related transactions. In the August 1990 Appraisal Availability Study, the Subcommittee presented the following findings:
    - there is wide diversity among the states on the degree of information available to appraisers;
    - public disclosure of information is dependent upon the individual state's real estate transfer recording statutes and practices;
    - the quality of appraisals depends to a large degree on the quantity and quality of public information; and,
    - real estate appraisers have had to rely to a great degree upon private sources of information to complete appraisal assignments.

- In March 1991, the ASC submitted to Congress a Personal Property Appraisal Study. The Study concluded that, while it would be feasible to extend to the personal property appraisal function a simple, generic regulatory structure similar to Title XI's regulatory structure for real estate appraisals/appraising, such an extension would not be desirable.

    b. What have been the results of any efforts ASC has undertaken using this authority?

Response: The National Registry was successfully redesigned and went public on January 1, 1998. The Appraisal Data Availability Study was submitted to Congress in August 1990.

The Personal Property Appraisal Study was submitted to Congress in March 1991.

3. During the 2000s, two prominent issues were appraisal fraud and pressure on appraisers by mortgage originators and others to hit targeted values.

    a. What did ASC do to address these two prominent issues?

Response: The ASC, through its monitoring of the States' appraiser regulatory programs, supports State agencies' efforts to address mortgage and appraisal fraud. The ASC monitors States' enforcement programs for processing and investigating of complaints, and sanctioning appraisers in a timely, effective, consistent, equitable, and well-documented manner. Complaints against appraisers must be processed within a one-year timeframe, absent special documented circumstances that would warrant an extension of that time. This would include complaints of fraudulent, incompetent or otherwise misleading appraisal reports. This also includes complaints regarding appraisers who misrepresented their appraisal conclusions by "hitting targeted values" or otherwise misrepresenting the characteristics of the subject property. The ASC has also encouraged States to join multi-agency fraud law enforcement task forces and report suspicious activity to appropriate law enforcement agencies. Effective enforcement at the State level is essential for addressing appraisal fraud.

The ASC supports efforts by the Appraisal Foundation to emphasize appraiser independence and the importance of promulgating appraisal standards that are understandable and enforceable, which is critical to the States' ability to effectively supervise appraisers within their jurisdiction. Effective supervision is a key component to minimizing appraisal fraud and misrepresentation. For example, the ASC staff was supportive of the Uniform Standards of Professional Appraisal Practice (USPAP) change in 2010 requiring appraisers, prior to accepting an assignment, to disclose any services they performed during the past three years on a property they are currently appraising. This disclosure is important to establish that the appraiser is exercising independent judgment and minimizes the potential for a conflict of interest.

It should be noted that the ASC has no authority to address instances where parties to a federally related transaction pressure appraisers to misrepresent the conclusions in their appraisal reports. However, once the appraisal complaint hotline is operational, appraisers, consumers, and other entities will be able to forward complaints of appraiser independence and violations of USPAP to the hotline for subsequent referral to the proper authorities. Establishment of the appraisal complaint hotline is being given priority by the ASC during FY 2012. ASC staff anticipates that the hotline will be operational prior to the close of FY 2012 (September 30, 2012).

    b. To what extent did these issues arise during ASC's compliance reviews of state appraiser regulatory agencies?

Response: During the State Compliance Review, ASC staff asks the States about complaints involving potential mortgage fraud. This question is a way for ASC staff to engage in a discussion with the States and encourage them to refer any potential fraud cases to the appropriate law enforcement officials. ASC staff also encourages the States to become involved in multi-agency fraud law enforcement task forces.

4. ASC is part of the Federal Financial Institutions Examination Council (FFIEC), which is comprised of the Federal banking regulators.

    a. What are the advantages and disadvantages of this arrangement in terms of ASC's ability to monitor the appraisal regulatory structure?

Response:

While the ASC is a Subcommittee of the FFIEC, it should be noted that the ASC membership and that of the FFIEC are not the same. The ASC includes two member agencies, the Department of Housing and Urban Development (HUD) and the Federal Housing Finance Agency (FHFA), which are not part of the FFIEC.

Title XI provides the FFIEC authority over the ASC in four specific instances. The four areas of authority are:

- Selecting the ASC Chairman for a 2-year term.
- Approving annual National Registry fee increases above $40.
- Approving temporary waivers issued by the ASC of appraiser certification or licensing requirements for States having a scarcity of qualified appraisers.
- Approving an extension (up to an additional 12 months) for State requirements for the registration and supervision of appraisal management companies if the ASC makes a written finding that a State has made substantial progress in establishing a State appraisal management company registration and supervision system that appears to conform with the provisions of Title XI.

Historically, the ASC Chairman provided updates on activities at the FFIEC meetings. The ASC's projects were included in the FFIEC's project reports and the ASC's members and relevant statutes were included in the FFIEC's annual report. In 2003, however, the FFIEC's external auditor raised concerns about whether the ASC should be incorporated into and reflected in the FFIEC's financial statements. After review, the FFIEC subsequently concluded that the ASC was independent of the FFIEC and should not be consolidated into the FFIEC's accounting or official reports. The FFIEC members agreed that the FFIEC could request a briefing from ASC at an FFIEC meeting if they had questions or concerns related to the adequacy of the requirements established by the agencies to govern appraisal standards or appraisal processes. In addition, the ASC Chairman and its executive director have provided briefings from time to time to FFIEC's Task Force on Supervision. Since 2004, however, direct interaction between the FFIEC and the ASC has been limited. ASC operations are fully funded by National Registry fees paid by State licensed and certified real estate appraisers. The ASC creates its own budgets and submits those budgets to the Office of Management and Budget. During 2011, the Chairman of the FFIEC has shown a particular interest in ASC activities, due in part to the additional authority and responsibility given to the ASC in the Dodd-Frank Act. There are advantages and disadvantages to the current arrangement.

Advantages: The composition of the ASC provides the opportunity for member agencies to share information among themselves and with the ASC staff regarding each agency's appraisal regulatory activities, individually and from an interagency perspective. The recent addition of the FHFA and the Consumer Financial Protection Bureau (CFPB) as member representatives to the ASC provides additional perspectives for the monitoring and enforcement functions the ASC provides. For example, the FHFA has insight into appraisals included in loans sold to two of the government sponsored enterprises (Fannie Mae and Freddie Mac), whereas the CFPB will bring a consumer protection oriented viewpoint to the ASC. Information obtained by ASC staff and board members as part of the State Compliance Review process and monitoring of the Appraisal Foundation can also be useful for the federal financial institution regulators, HUD and FHFA as they consider appraisal policy and enforcement.

Disadvantages: Information sharing is restricted and limits the ability of the member agencies to share information deemed pre-decisional with other ASC members and the ASC staff.

b. To what extent does this structure allow ASC to be proactive in identifying and addressing emerging issues in the appraisal industry?

Response: The structure does provide opportunities for the ASC to be proactive in identifying and addressing emerging issues in the appraisal profession. For example, individual ASC members brought to the attention of the Appraisal Foundation their observations regarding the absence of guidance on best practices for appraising in declining markets. The Appraisal Foundation independently determined that such guidance was needed and has since constituted the Appraisal Practices Board (APB). The primary mission of the APB is to address emerging issues where national level guidance is warranted.

While the composition of the ASC has included the federal financial institution regulatory agencies responsible for supervising real estate lending and appraisal practices of federally regulated institutions and HUD, the addition of the FHFA and CFPB offers even more opportunity to be proactive, and broadens the perspective of the ASC regarding issues of national appraisal policy and enforcement of Title XI. With the ASC's new rulemaking authority, member agency rulemaking experience in issuing joint rules could be useful. Member agency experience with complaint hotlines and grant administration could also be useful.

5. The Dodd-Frank Act grants ASC new authorities and functions, including limited rulemaking authority, the ability to make grants to states, and the establishment of a national appraisal complaint hotline.

a. To what extent does ASC have the capacity to undertake these new authorities?

Response: The ASC is currently developing a Strategic Plan to address the new authority pursuant to the Dodd-Frank Act. The Strategic Plan should be completed by the end of 2011. ASC will need additional staff resources to address these new authorities and will require additional funding. This need was partially addressed by the Dodd-Frank Act that authorized the ASC to raise the annual National Appraiser Registry fee to $40 from the current $25. The increase is effective January 1, 2012, and will provide the ASC with additional resources to carry out its new authorities. Once the Strategic Plan is finalized, the ASC will address any additional staffing or other operational needs. Further staffing increases may be needed to address the new rulemaking authority and monitoring the requirements established by the States for the registration and supervision of appraisal management companies (AMCs).

b. What is the status of ASC's actions to fulfill these responsibilities, and what are ASC's timelines for implementation?

Response: The ASC is diligently moving forward with the implementation of various provisions within the Dodd-Frank Act, including:

- The ASC approved an increase in the National Registry fee to $40 effective January 1, 2012.
- ASC implemented open meeting provision of the Dodd-Frank Act.
- The Federal Housing Finance Agency took its seat on the ASC.
- Updated internal ASC Policies and Procedures were implemented.
- The ASC determined that no appraisal complaint hotline existed that satisfied the criteria in Title XI as amended. Staff is currently conducting research on establishment and operation of complaint hotline (target date FY 2012).
- The ASC issued a Bulletin to the States informing them of the statutory requirements and the effective date for ASC monitoring for compliance:
    - Appraiser Credential Reciprocity between States (effective 7/1/13)
    - Certification and licensing requirements for State licensed appraisers (effective 7/1/13)
    - Certification and licensing requirements for trainee and supervisory appraisers (effective 7/1/13)
    - Encouraging the State to accept appraisal courses approved by the AQB Course Approval Program (effective 7/1/11)
    - ASC monitoring State Programs for the purposes of determining whether a State has policies, practices, procedures, *funding*, and *staffing* consistent with the purpose of Title XI (effective 7/1/13). Funding and staffing oversight authority is new per Title XI as amended.
- Annual Report transmitted to Congress as required.
- The ASC approved a request from Idaho to extend the effective date for the National Registry fee increase, and offered the same to any State able to show they are unable to meet the effective date due to extenuating circumstances.

The following Dodd-Frank Act provisions are currently being studied and prioritized. They include:

- State grants to be administered after policies are established (target date FY 2012).
- Establish rulemaking policies and procedures (target date FY 2012).
    - Additional State sanctioning authority
    - National Registry
    - Information Sharing
    - Enforcement
    - Temporary Practice
- Establishing policies and procedures for monitoring States' laws, regulations and policies regarding appraiser independence (target date after FY 2012).

Concerning ASC monitoring of State registration and supervision of AMCs, prior to this action, the federal financial institution regulators, the CFPB, and the FHFA are required to issue regulations setting the minimum requirements for State registration of AMCs within 18 months after the designated transfer date as established pursuant to the Dodd-Frank Act. Once those regulations are in final form, States have 36 months to implement the federal requirements at a minimum. The ASC has the authority to grant a 12-month waiver for States that can show substantial progress toward implementation. Due to this statutorily imposed timeline, the ASC will not begin work on an AMC registry for at least 1-2 years.

6. Please describe your understanding of the authority of TAF to create the Appraisal Practices Board and the decision making process that led to TAF create the Appraisal Practices Board.

Response: The Appraisal Foundation (Foundation) is a private 501(c) (3) corporation. Relative to Title XI, its congressional authority is limited to establishing minimum appraisal standards and qualification criteria for real estate appraisers. However, the Foundation is not limited to its Title XI-related functions. For example, recognizing that appraisals are completed for interests outside of real property and in the interest of public trust in the appraisal profession as a whole, the Foundation has chosen to write voluntary standards for personal property appraisers and business valuers. Similarly, the Appraisal Foundation recognized that there is void in the marketplace of generally accepted appraisal practices. USPAP requires appraisers to develop appraisals using "recognized methods and techniques." However, there currently is no set of authoritative "best practices" or "recognized methods and techniques." Therefore, the Foundation independently decided to constitute a separate Board, the Appraisal Practices Board (APB). Because Title XI does not give the Foundation the authority to establish "best practices", and because it does not authorize the ASC to grant monies to the Foundation for such activities, no federal funds are being used for the APB. The Foundation should be consulted for more details specifics regarding the decision making process that led the Foundation to create the APB.

7. The Dodd-Frank Act requires that the State agencies that regulate appraisers also regulate Appraisal Management Companies (AMCs).

    a. How, if at all, is ASC working to ensure that AMCs and independent appraisers are regulated objectively?

Response: As a point of clarification, Title XI provides that States may establish appraiser certifying and licensing agencies. As amended by Dodd-Frank, those State agencies may register and supervise AMCs.

Concerning ASC monitoring of State registration and supervision of AMCs, prior to this action, the Dodd-Frank Act requires the federal financial institution regulators, the CFPB and FHFA to issue regulations setting the minimum requirements for State registration. The minimal timeline set forth in the Dodd-Frank Act indicates that those regulations may be promulgated within 18 months of July 21, 2011 (January 2013). Once those regulations are in final form, States have 36 months to implement the federal requirements. ASC staff anticipates that the AMC Registry and monitoring of States' registration and supervision of AMCs will be implemented along with the State's establishment of AMC registration in accordance with the regulations.

As part of the ASC Compliance Review process, the ASC requires State agencies to ensure that processing and investigation of complaints and sanctioning of appraisers is administered in a timely, effective, consistent, equitable, and well-documented manner.

b. Is the regulation of AMCs and/or independent appraisers effective?

Response: Prior to ASC monitoring of State registration and supervision of AMCs, the federal financial institution regulators, the CFPB, and the FHFA are required to issue regulations setting the minimum requirements for State registration of AMCs. This must be accomplished within 18 months after the designated transfer date as established pursuant to the Dodd-Frank Act. Once those regulations are in final form, States have 36 months to implement the federal requirements at a minimum. The ASC has the authority to grant a 12-month waiver for States that can show substantial progress toward implementation. Due to this statutorily imposed timeline, the ASC will not begin work on an AMC registry for at least 1-2 years.

No further comment is possible on AMC regulation until that rulemaking process is complete.

Given the framework initially provided by Congress in Title XI, regulation of appraisers has been relatively effective. While State appraiser regulatory agencies continue to suffer from a lack of resources in many cases, the amendments to Title XI by the Dodd-Frank Act provide an opportunity to improve on and enhance appraiser regulation.

New CFPB Mortgage Disclosures Win Praise for Content and Process

American Banker | Thursday, May 19, 2011

By Kate Davidson

WASHINGTON - The Consumer Financial Protection Bureau's prototypes for a single mortgage disclosure form won praise from industry groups Wednesday for their streamlined format, as well as the unorthodox way they are being developed.

Under the Dodd-Frank Act, the CFPB does not have to issue a final version of the form until July 2012. But the bureau has already invited industry representatives, bankers and consumer advocates to weigh in on the model forms, which will be tested on focus groups and revised throughout the summer before the formal rulemaking process even begins.

"I think what was probably the most refreshing was just the fact that you had a room of bankers there ... folks who use this every single day and have to explain it to customers every single day," Ron Haynie, the president and CEO of ICBA Mortgage, said about a meeting with CFPB officials this week. "And the folks at the CFPB were asking questions - does this work? They want the feedback, and bankers are not a shy bunch."

Haynie and other industry observers said the two prototypes released Wednesday are a good first step toward merging the disclosure forms required under the Truth in Lending Act and Real Estate Settlement Procedures Act.

"Our bankers felt that this was clearer, more to the point, and was a substantial improvement" over existing disclosure forms, said Bob Davis, executive vice president of government relations for the American Bankers Association, who also met with CFPB officials and several bankers on Tuesday. "So they welcomed seeing this."

Each form has a slightly different design (see them here<http://www.consumerfinance.gov/wp-content/uploads/2011/05/disclosure1.pdf> and here<http://www.consumerfinance.gov/wp-content/uploads/2011/05/disclosure2.pdf>), but both would break down the mortgage offer to highlight key terms, such as interest rate and monthly payment, and would caution borrowers about certain terms, such as increasing loan amounts or balloon payments.

Both also include a section to help consumers compare the offer with other loans, and lays out projected payments over the life of the loan. They break down expected closing costs, and use check boxes to indicate whether a loan requires an escrow account or mortgage insurance.

Although it was still early, the reviews for both forms were positive.

Stephen Ornstein, a partner at SNR Denton, said the forms are and easy to understand. The section for projected payments and "cautions" is particularly helpful.

"As jaded a compliance attorney as I am, I think they're terrific," Ornstein said. "Particularly the first one."

Norma Garcia, a senior attorney with the Consumers Union, agreed.

"They both do a great job of laying out the essential information. However, I think disclosure 1 is easier to navigate," Garcia said. "It's visually easier to break the essential information into parts that make it easy for a consumer to digest."

Industry representatives were also pleased.

"It seems like they're trying to make an effort to have things that are clear to the eye, and also to use language that consumers understand," said Elizabeth Eurgubian, a vice president and regulatory counsel at the Independent Community Bankers of America. "That being said, they're not there yet. But the process has started."

David H. Stevens, the president and CEO of the Mortgage Bankers Association, said in a press release Wednesday that the CFPB staff put a lot of thought into the new forms, and the MBA looks forward to participating in the revision process.

"One of MBA's primary goals will be to make certain that not only do the new forms provide consumers with the information they need in a simple, clean way, but also that they can be implemented into lenders' operations and systems with a minimum of disruption," he said.

Stevens also noted that the industry "expended considerable costs" on Respa changes just 18 months ago.

"We need to make sure that this new form is highly beneficial to consumers who will bear the implementation costs," he added.

The Dodd-Frank Act directed the CFPB to merge the TILA and Respa forms, which are two and three pages long, respectively, and have overlapping information.

The bureau plans to test the prototypes with focus groups before beginning a formal rulemaking process. It will conduct five rounds of evaluation and revision through September 2011 to select a single draft disclosure and then refine it.

"We're just going to keep testing this thing," Elizabeth Warren, the administration's point person in charge of setting up the CFPB, said in a conference call with reporters on Wednesday. "We're going to listen to comments, adjust and retest, until, with lots of help from the public, from industry, we believe we have this right."

Some were optimistic that the CFPB's process will set the standard for how the new agency develops rules in the future.

"This shows the CFPB wants to make regulation work better, because they're rolling these out early, they're showing them to bankers and consumers, they're going to be testing them, and this is doing regulation better," said Edmund Mierzwinski, the consumer program director at the U.S. Public Interest Research Group. "It's not more government, it's better government. So that's I think the exciting thing."

Reaching out to the public so early in the process is something that no other federal agency, and certainly no banking regulator, has ever done before, said Travis Plunkett, a legislative director at the Consumer Federation of America.

"To me this is a model for what the consumer bureau can become, in terms of reaching out to the public and getting input not just from the usual suspects - and that includes us, by the way - but from borrowers affected by the regulations that they're considering," Plunkett said.

Richard Riese, director of the ABA's Center for Regulatory Compliance, said the bureau has tried to engage both bankers and consumer advocates on how to communicate useful information to consumers about their mortgage transaction. That allows stakeholders to focus first on the quality of the forms, rather than the legalese, Riese said.

"I think this, as Elizabeth Warren has said on numerous occasions ... is an approach that if they think it's producing good results and other people feel that the process was worth engaging in because of those results, then it could be applicable in future standard settings," Riese said.

There may be some risk to the open nature of the process, especially because it doesn't follow normal rulemaking protocols, Riese said.

"But it doesn't mean that they won't get to the normal process down the line to ensure that the legal hurdles have been met," he said. "It's that she is enabling people to see ... more of the sausage-making that goes into how you get to a more formal proposal."

The bureau also plans to conduct additional analysis and research over the summer, and consider underlying regulatory issues and ways to refine closing-stage mortgage forms, a process that will likely extend into the fall and early next year.

CFPB must issue the proposed forms and regulations for formal notice and comment by July 2012.

SPENCER BACHUS, AL, CHAIRMAN

United States House of Representatives
Committee on Financial Services
Washington, D.C. 20515

BARNEY FRANK, MA, RANKING MEMBER

March 24, 2011

The Honorable Ben S. Bernanke
Chairman
Federal Reserve Board
20th & Constitution Ave. NW
Washington, DC 20551

Federal Reserve Final Rule on Loan Originator Compensation
Regulation Z: Docket No. R-1366, Truth in Lending

Dear Chairman Bernanke:

I am writing to urge that the Federal Reserve take immediate action to make two changes to the rule cited above, which is scheduled to take effect on April 1st.

It is important at this point that the rule take effect, and that the Federal Reserve immediately thereafter amend the rule to make these two changes. I urge these changes both for substantive reasons and to dispel the misperception that all the elements in the rule were called for under the "Wall Street Reform and Consumer Protection Act" (P.L. 110-203) (or as it is sometimes referred to, as the Financial Reform Act).

As the Federal Reserve noted in its September 24th rule publication, much of the rule is consistent with the Financial Reform Act. However, I believe it was a mistake for this rule to go beyond what was required in the Financial Reform Act. The two problems I am citing unnecessarily interfere with borrowers' ability to obtain loans from mortgage brokers and their resolution would not damage the core underlying consumer protections. Therefore, I believe it is important that the rule take effect as scheduled, and that the Federal Reserve take immediate action to correct the two problems created by the rule.

First, the rule appears to prohibit a mortgage brokerage firm that is receiving compensation for a loan from the consumer from paying any compensation related to that loan to an employee of that firm. This is because the rule appears to include language that states that when a loan originator receives compensation from the consumer on a loan, no loan originator at all can receive compensation related to that loan from any source.

This differs from Section 1403 of the Financial Reform Act, which merely states that if a loan originator receives compensation from the consumer, that originator cannot receive compensation from another source. This statutory provision prevents double dipping, while the more restrictive Fed rule prevents the sharing of the consumer-paid compensation by the firm with an employee for that employee's work on the loan. I would note that such sharing of compensation would not involve an increase, directly or indirectly, in the level of fees paid by the consumer. I believe this language should be revised to allow employee compensation in this circumstance. Of course, any such compensation should be subject to

Page Two

the same rule as laid out in the Rule of Construction (A) in Section 1403 of the Financial Reform Act – that such compensation cannot vary based on terms of the loan, other than the amount of principal.

The second issue relates to a common occurrence in which mortgage brokers offer to make small fee reductions at loan closing, to cover shortfalls which sometimes result because of last minute third party fee changes, or to cover the cost of a short extension of a loan lock when the loan failed to close within the window of the original loan lock. I believe this practice should be allowed if the fee reduction is at the request of the borrower and is made within a short period (eg., 24 hours) of the loan closing. I believe that permitting such a practice does not undermine the rule's essential consumer protections. However, I am cognizant of the potential for a loan originator to systematically make use of such a practice with the intent of circumventing the rule's consumer protections. Therefore, it would be appropriate to limit the frequency of such use and to limit either the dollar or percentage amount of the reduction, and to monitor a loan originators' use of this flexibility to ensure that such flexibility is not abused.

I believe that both of these provisions should be revised expeditiously by the Federal Reserve through an appropriate action or proceeding at the earliest possible time.

Thank you for your consideration of these requests.

BARNEY FRANK
Ranking Member